



NEW AMERICA
FOUNDATION

Helping Consumers Make Wise Financial Decisions

*A Report from a Roundtable on the State of Financial Education
as it Relates to Public Policy*

**Financial Services and Education Project
Asset Building Program**

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INTRODUCTION

The U.S. financial system has changed radically over the past few decades. More than ever before, consumers are required to take personal responsibility for managing their finances, making investment decisions, selecting from a proliferation of financial products and services, and planning their retirement. Consumers must decipher information about a multitude of financial products and services to determine which options best meet their needs. For many, the sheer number of these options is overwhelming.

The impact of the combination of increased personal responsibility and an increasingly complex financial system is beginning to show in the form of increased financial distress. Most consumers do not have the tools they need to navigate this system and make wise decisions. As a result many are accumulating high levels of debt and saving very little. Predatory lending and other practices designed to take advantage of consumer confusion further compound the problem. Many families are just one crisis away from a financial emergency. Loss of employment, health issues, and family emergencies, ranging from unexpected car repairs to divorce, can push a financially fragile family over the edge. While the most dire impact is on families with lower incomes and few assets, in fact the concern is far more widespread.

The lack of financial competency has become a national concern that threatens America's global competitiveness. When consumers lack access to the information and supports that help them make wise decisions, there are serious consequences not only for the consumer, but also for the financial services industry and the country's economy as a whole. A nation of financially stressed workers and an older population unable to support itself is not a recipe for international competitiveness. If people are able to decrease their debt and save more money, they can become more financially stable. Better financial health leads to more competitiveness in the global marketplace. We need policies that support consumers' ability to make wise financial choices. Effective financial education is one of those policies.

On March 21 and 22, 2007, the Financial Services and Education Project of the Asset Building Program at the New America Foundation hosted a roundtable discussion among a diverse group of people with expertise in financial education. The group included academics from a variety of disciplines, those involved in providing financial education for both youth and adults, representatives of financial institutions, and others interested in the topic. This paper briefly summarizes two days of rich discussions. In the near future, we will publish a series of policy recommendations informed by the roundtable that we believe can begin to help Americans be fully competent to succeed in a world of increased financial responsibility and opportunity.

A MULTIFACETED SOLUTION—FIVE KEY ELEMENTS

Consumers are having difficulty making wise financial decisions for several reasons. The financial services system has become much more complex, our culture promotes consumption over saving and investment, and the “democratization of credit” – while overall a good thing – has opened the door to sophisticated marketers who skillfully promote products and services that encourage consumers to “buy now and pay later.” Because myriad issues contribute to consumers’ difficulty in managing their finances effectively, a multifaceted solution is necessary. Financial education is an important part of the solution, but a more comprehensive approach is needed.

Based on the roundtable discussion, we suggest that the following five key elements would help consumers make wise financial decisions. Consumers need financial education, consumer-friendly products and services, financial institutions that encourage positive financial outcomes, increased consumer protections, and more and better trained providers of financial education, especially to low-income or low-wealth Americans.

Financial Education

Roundtable participants were in agreement that financial education should be provided and reinforced throughout a person’s life. To do this comprehensively requires: segmenting consumers so as to better match financial education to consumer needs; identifying and implementing the best financial education strategies for particular situations; improving the delivery of financial education; helping consumers understand when to seek advice or redress, and providing such systems; and moving consumers beyond financial knowledge to financial capability.

Segmenting Consumers

People think and learn differently, so it is important to consider different audiences when developing financial education programs. Programs should be based on consumer needs. Some consumers spend too much. Others are struggling to manage low incomes. Both groups could benefit from financial education, but each has unique needs and motivations. Age differences exist as well. For example, younger consumers tend to prefer online information, while older consumers want printed material. As a result, both high-tech and high-touch approaches are necessary, and multiple learning techniques are needed to reach different segments.

Identifying and Implementing a Variety of Intervention Strategies

Roundtable participants identified two potential models for classifying intervention strategies. The first model groups financial interventions into two categories: prevention and intervention. A prevention approach helps consumers avoid future financial trouble. An intervention approach helps consumers who are experiencing financial problems.

The second model analogizes financial problems to medical problems. Consumers might have an “emergency” financial challenge that requires immediate attention. Others might have a problem that they can handle on their own, so they choose to “self-medicate.” Some consumers might understand the basics of financial education, but periodically need a checkup from a “general

practitioner.” Still others need a “specialist” for guidance about a specific product or investment strategy.

The key point is that, whatever the model, a variety of strategies is essential, geared to the particular needs and competencies of individual consumers. Both group (including classroom, for youth) and individual interventions will be needed.

Improving the Delivery of Financial Education For Adults

Many programs that provide general financial education have struggled to attract and retain participants in the program. On the other hand, when the education is linked to a crisis or a specific goal, such as homeownership, saving for college, or planning for retirement, adults are often more motivated to participate. General financial education gives consumers a broad understanding of money management basics, but more innovative approaches that are more likely to be effective include product-specific information, pre-decision education, and point-of-sale education.

Product-specific information helps consumers understand the terms, costs, and risks of a particular product and helps them decide whether it meets their needs. Pre-decision education, like a homebuyer education class, helps consumers decide whether the particular financial decision they are making meets their long-term objectives. Point-of-sale education is provided to help consumers during a specific financial transaction.

The effectiveness of point-of-sale education should be explored further. Some participants suggested that, especially with houses and other products that people tend to get attached to before they buy, point of sale is too late to provide education. Others believe that people are not genuinely interested in education unless it's about their current finances; therefore, point-of-sale education could be important.

For Youth

Most high school graduates lack basic personal financial skills. Roundtable participants urged that financial education be taught in schools using tools such as bank accounts that will make that education relevant, and that teachers be trained to provide financial education.

Financial education should be taught starting at the kindergarten level and reinforced in every grade through high school. It should be integrated into the existing kindergarten through eighth-grade curricula, incorporated in core high school courses (in particular math and science), and included in each state's standardized testing. Roundtable participants noted that many teachers are not comfortable teaching financial education, and that pre-service education will give them the information and the confidence they need to teach this information.

Helping Consumers Understand When and How to Seek Advice or Redress

An important component of financial education is helping consumers understand when they should seek advice and who they can turn to for unbiased information. Financial education should help consumers deal with bad choices and understand their options for redress and recourse when things go wrong.

Over time, most all consumers will experience a situation where they need financial advice or want to dispute a charge or fee. Some participants noted that low-income consumers in particular are less likely to seek these solutions. For example, a low-income consumer might be charged an interest rate that seems unusually high. Although the consumer knows the rate is high, they somehow feel they “deserve” the higher rate because of their income level and they are less likely to dispute it. A system to help consumers access advice and empower them to seek redress when necessary is needed. New types of counseling systems may be required, in addition to enhancement of those that already exist. Participants pointed out that upper income consumers have access to this type of assistance in the form of financial planners, accountants, lawyers and brokers—and generally know when to call on them.

Moving Consumers Toward Financial Capability

Several participants advocated focusing not just on financial education, but also on financial capability. Financial capability focuses on developing the skills and confidence that consumers need to become more aware of financial risks and opportunities, to make informed choices, to know where to go for help, and to take other effective actions to improve their financial well-being. Achieving financial capability requires that education be accompanied by real-time practice with accounts and other financial products that enable consumers to evaluate and make choices in a safe setting.

Consumer-Friendly Products and Services

Factors other than knowledge of the financial system influence the decision-making process. Research discussed at the roundtable has shown that the probability of doing something is not related to the strength of intention as much as it is to the ease of doing it. People are overwhelmed with daily tasks and need manageable contexts and reminders.

One way to address this issue is to create consumer-friendly products and services through the power of defaults. A default is the option that is automatically selected unless an alternative is specified. Changing the default does not take away consumer options. Instead, the default is the option that policy makers have determined benefits most people. People who prefer another option have the opportunity to reject the default.

Most people keep the default option that is suggested to them; therefore, switching the default option can have a profound effect. For example, recent changes to US pension law encourage employers to automatically enroll their workers in 401(k) retirement plans—the default is changed from opt in to opt out. Pre-enactment experimentation suggested that the change from opt in to opt out increased participation among low-wage workers from 13% to 80%. Other examples discussed for changing the default option for financial products to encourage better decisions were credit and spending products with automatic savings features and making a

limited-access savings account the default first account for consumers.

Encourage Financial Institutions to Promote Positive Financial Outcomes

Financial education in isolation will not necessarily lead to positive financial decisions. The manner in which financial institutions interact with consumers can encourage or discourage good results. Currently, the financial services playing field is uneven. Sophisticated marketers and sellers are promoting complex products to a much less informed consumer base.

Participants had several suggestions to improve the way financial institutions interact with consumers. The most basic was that financial institutions need to better understand what consumers want, and provide it—being listeners rather than sellers and taking responsibility for positive outcomes for consumers. Another suggestion was that financial institutions provide advice before consumers get into trouble. In particular, lenders can use credit scores and modeling to identify customers who face potential financial trouble and intervene with education or other assistance to keep them out of trouble—rather than the current situation in which high-risk customers are often solicited for additional credit products. Similarly, buyer’s brokers and other forms of trusted advisors should be available to lower income consumers.

Research, policy and regulatory change can encourage this kind of rethinking of the role of the financial institution. Embedding this philosophy into the services test of the Community Reinvestment Act is one approach that participants suggested should be considered.

Increased Consumer Protections

For many reasons, including the ease and speed with which financial products change, consumer protections often lag problems and clearly are not the complete solution to helping consumers make wise financial decisions. However, they have an important role to play. Roundtable participants proposed the following specific consumer protection ideas:

- Eliminate consistently detrimental components of certain products, such as universal default and over-the-limit fees on credit cards.
- Incorporate existing consumer protections into new products quickly, for example clarifying Federal Deposit Insurance Corporation (FDIC) insurance on prepaid card products.
- Provide the same loss-limit protections for debit cards as exist for credit cards.
- Require consumers to consent before providing overdraft privileges on debit and prepaid cards.
- Underwrite credit products at the fully indexed interest rate, rather than a teaser rate.
- Prohibit certain especially hazardous products, like credit life insurance.
- Provide all disclosures in clear, concise language written at a seventh-grade reading level.

More and Better Trained Providers of Financial Education to Low-Income or Low-Wealth Americans

There are many individuals providing financial counseling today for low-income or low-wealth Americans. However, they are concentrated in credit counseling, helping those already in

serious difficulty; homeownership counseling; and working with Individual Development Accounts. Not only are more dedicated counselors needed, but people who regularly interact with low-income or low-wealth consumers need to be trained to provide good financial advice. Four suggestions made at the roundtable were (1) creating a financial counseling corps of volunteers, (2) training those who work with low-income employees, (3) establishing financial counseling accreditation and certification, and (4) encouraging financial education at work.

Creating a Financial Counseling Corps of Volunteers

Roundtable participants suggested that the number of available advisors, potentially including people with significant experience in the financial services industry, could be increased by establishing a Financial Counseling Corps to train, place and coordinate volunteer advisors. Volunteer efforts can be expensive and difficult to manage, so it would be important to learn from other models and similar efforts, such as SCORE (Service Corps of Retired Executives), AmeriCorps, or the Peace Corps.

Training Those Who Work with Low-Income Families

Individuals who work with low- and moderate-income consumers—like educators, social workers, and financial institution employees—have a unique opportunity to provide financial education, and to provide it in a “just in time” context that increases the likelihood of success. However, roundtable participants noted that these individuals often lack the knowledge, skills and confidence to help. If properly trained, they could form an important delivery system to provide financial education information to their constituents.

Establishing Financial Counseling Credentials and Certification

Consumers need to be able to identify quality financial education trainers and programs. A certification and credentials program could be developed for financial education providers working with low-income families. Once a certification and credentials program is in place, financial education programs could offer credentialed counselors and educators who have the official designation (e.g., recognition similar to “Energy Star” or the “Good Housekeeping Seal of Approval”). Participants recognized that credentialing programs can be difficult to administer in a way that does not unduly restrict the supply of advisors, but suggested the concept was worth further exploration.

Encouraging Financial Education at Work

Roundtable participants noted that many employers are motivated to provide financial education to employees, for a number of reasons ranging from reducing employee stress to providing employees with a good alternative to the payday advances small employers are often asked for. However, employers are not sure how to go about this, and many employees are reluctant to open their entire financial situation to their employer. Several on-going initiatives demonstrate the value of the workplace as a delivery location for financial education. Especially for smaller employers, roundtable participants suggested a need for incentives to encourage private employers to provide broad-based, comprehensive financial education.

AREAS FOR ADDITIONAL RESEARCH

Roundtable participants highlighted several areas for further exploration to develop a comprehensive approach that can help consumers make good financial decisions. Three primary research areas are (1) understanding consumer demand, (2) exploring consumer motivations and effective marketing approaches, and (3) incorporating best practices from other fields.

Understanding what the consumer wants is critical. This includes better understanding both what consumers say they need and what kinds of products and services can help them meet those needs in a sustainable way. We also need to better understand how to design programs and products in a consumer-friendly context that helps consumers make wise decisions that move them along the financial continuum to asset building and retention.

A second area for exploration is to learn more about marketing and motivation. We need to better understand the marketing approaches that are most effective and that address key consumer motivations. Understanding how and when to tap into consumer preferences with different marketing approaches, such as the use of fear, motivation, and incentives, will enable those in the industry, including community based organizations, that are providing good products to break through the ubiquitous availability of products that are less than ideal.

Finally, much can be learned from other fields to help consumers make sound decisions. Information from fields such as psychology, neuroscience, behavioral economics, health, nutrition, family sciences, and child development can yield important and relevant information to improve financial capability and decision-making.

CONCLUSION

Today's financial services system challenges all American consumers to take greater individual responsibility for their financial activities and security—in an environment that is increasingly complex. Enabling consumers to make the best possible choices is a multifaceted activity, of which formal financial education or counseling is only one part. The roundtable explored how to improve the content and delivery of financial education to maximize consumers' financial capability. Some of the activities suggested can and should be undertaken without any change in public policy. Others either require or will be enhanced by policy changes. We intend to continue the roundtable discussion, and have added a financial education section to www.assetbuilding.org. And the roundtable discussion will form the platform on which the New America Foundation will work with others to develop and implement changes in public policy that will help all Americans become more fully able to get the best long-run financial performance for themselves and their families.

Appendix. List of Participants

Michael Beacham

Money Savvy Generation

Ted Beck

National Endowment for Financial Education

Ray Boshara

New America Foundation

Stephen Brobeck

Consumer Federation of America

Michael Calhoun

Center for Responsible Lending

Sharon Danes

University of Minnesota

Dara Duguay

Citigroup Office of Financial Education

Jean Ann Fox

Consumer Federation of America

Patty Hasson

Consumer Credit Counseling Service of Delaware Valley

Margaret Henningsen

Legacy Bank

Sharon Hermanson

AARP

Jeanne Hogarth

Board of Governors of the Federal Reserve System

Beatriz Ibarra

National Council of La Raza

Lissa Johnson

Center for Social Development

Kathryn Kelly

American Bankers Association Education Foundation

Melissa Koide

New America Foundation

Laura Levine

The Jump\$tart Coalition for Personal Financial Literacy

Annamaria Lusardi

Dartmouth College

Lewis Mandell

The State University of New York University at Buffalo

Ben Mangan

EARN

David Marzahl

Center for Economic Progress

Brandee McHale

Ford Foundation

Karen Murrell

New America Foundation

Brent Neiser

National Endowment for Financial Education

Leslie Parrish

Center for Responsible Lending

Jane Schuchardt

U.S. Department of Agriculture

Ellen Seidman

New America Foundation

Eldar Shafir

Princeton University

Margaret Sherraden

Center for Social Development

Irene Skricki

The Annie E. Casey Foundation

Barbara A. Smith

Federal Reserve Board

Jonathan Sprague

Financial Planning Association

Lois Vitt

Institute for Socio-Financial Studies

Geoff Wilson

Junior Achievement