

Revised Draft

LATVIA

*Diagnostic Review of
Consumer Protection and
Financial Capability*

**Volume I
Key Findings and Recommendations**

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Diagnostic Review of Consumer Protection and Financial Capability

Volume I Key Findings and Recommendations

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Abbreviations & Acronyms

ADR	Alternative dispute resolution
AMC	Asset management company
APR	Annual Percentage Rate of Charge
B2B	Business-to-Business
B2C	Business-to-Consumer
CIU	Collective investment undertaking
COE	Council of Europe
CRPC	Consumer Rights Protection Center
DOLCETA	Development of On-Line Consumer Education Tools for Adults
DG SANCO	Directorate-General for Health and Consumers (of the EC)
DSI	Data State Inspectorate
EC	European Commission
ESIS	European Standardized Information Sheet
EU	European Union
EURIBOR	Euro Interbank Offered Rate
FCMC	Financial and Capital Market Commission
FX	Foreign Exchange
GDP	Gross Domestic Product
IADI	International Association of Deposit Insurers
IPO	Initial public offering
KYC	Know your customer
LCCUA	Latvian Association of Cooperative Credit Unions Association
LFMI	Law on Financial Markets Instruments
LIBOR	London Interbank Offered Rate
LVL	Latvian Lat
LTV	Loan-to-Value
MiFID	Directive on Markets in Financial Instruments
MOU	Memoranda of Understanding
MTPL	Motor third party liability
NBCI	Non-bank credit institution
NGO	Non-governmental organization
NMS	European Union New Member States
OECD	Organisation for Economic Co-operation and Development
PIAA	Latvian National Association for Consumer Protection
RIGIBOR	Riga Interbank Offered Rate
SSIA	State Social Insurance Agency
UCITS	Undertakings for Collective Investment in Transferable Securities
UK	United Kingdom
US	United States of America
USD	United States Dollar

n.a. Not Available

\$1 = 0.52 LVL (March 2010)

Foreword

Consumer protection in financial services lies at the heart of any financial sector that is efficient, competitive and fair. Three areas are important. Customers of financial institutions need to receive information that is clear, complete, accurate and comprehensible before they decide to borrow or to invest. They must have access to recourse mechanisms that are efficient and cost-effective. They need also to obtain sufficient financial education to understand the terms and conditions and other information provided to them as financial consumers.

We are pleased to provide this pilot Diagnostic Review of Consumer Protection and Financial Capability in Latvia and thank the Latvian authorities for their valuable cooperation and collaboration in its preparation. The Review not only looks at financial services in Latvia but also refines a set of Good Practices or benchmarks for use in reviewing consumer protection in financial services in any jurisdiction. It is expected that this work will prove helpful to the international community and those in emerging markets who seek to establish common ground for minimum Good Practices in consumer protection in financial services.

Acknowledgments

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Executive Summary

The global financial crisis has highlighted the importance of consumer protection and financial capability as medium-term measures supporting financial sector development. In addition to short-term measures to mitigate economic impacts, policymakers are taking steps to build better foundations for future development of the financial systems through improved regulatory reforms. These medium-term measures involve enhanced financial prudential regulation and oversight, financial sector governance (including governance of financial regulators and supervisors), business conduct regulation and supervision, and financial consumer protection. The latter receives an increasing emphasis not only in developed countries but also in emerging market economies, as most of the risk exposures associated with the latest credit boom were assumed primarily by households.

Financial consumer protection improves efficiency of financial intermediation—and indirectly reduces risks to financial stability. At its heart, consumer protection addresses power, information, and resource imbalances which place consumers at a disadvantage *vis-à-vis* financial institutions. Financial institutions are very familiar with the terms and conditions of their financial products and their risk characteristics. Retail consumers may find it difficult or costly to obtain sufficient information on their financial purchases or understand complex financial products even when relevant information is disclosed. Consumers who are empowered with information and basic rights—and who are aware of their responsibilities—provide an important source of market discipline to the financial sector, encouraging financial institutions to compete on the basis of useful products and services. In addition, financial consumer protection builds trust in financial systems and helps broaden and diversify the depositors' base. Such public confidence indirectly reduces the liquidity risk of the banking sector.

Consumer protection is gaining increasing importance at both the EU and Latvian level. The EU Consumer Policy strategy of 2007-13 sets three objectives. These are: (i) to empower consumers by ensuring that they have real choices, accurate information, market transparency, and the confidence that comes from effective protection and solid rights; (ii) to enhance consumers' welfare regarding price, choice, quality, diversity, affordability and safety of products; and (iii) to protect consumers as a group from serious risks and threats that cannot be withstood on an individual basis. An October 2008 report of the European Parliament also identified measures to be taken to improve financial education throughout the EU.

The years 2003 to 2008 saw rapid increases in levels of consumer debt in Latvia. Loans to Latvian households grew at an average annual rate of 80 percent in years 2004-2006 and then slowed down to annual growth rates of 39 percent in 2007 and 7 percent in 2008. Mortgage debt rose from 8 percent of GDP by end-2003 to 31 percent by end-2008—second in central Europe only to Estonia at 32 percent in 2008. Such high levels of household debt left the Latvian economy vulnerable to the global financial crisis. By June 2009, the Latvian economy had dramatically slowed with an 18 percent decline in output from the previous year and a 50 percent reduction in average housing prices in Riga.

Exacerbating the vulnerabilities were weaknesses in the levels of consumer protection and financial literacy. According to the October 2008 Eurobarometer survey of 27 EU Member States, only 35 percent of Latvians felt that they were adequately protected by general consumer protection measures (vs. 51 percent among consumers throughout the EU). Two years earlier in February 2006, a private survey of over 1,000 Latvian households found that a similar

percentage—46 percent—of consumers were concerned that they lacked sufficient knowledge about such basic issues as consumer credit.

While Latvia has adopted the required EU Directives, the institutional structures have had difficulty addressing the issues facing financial consumers. The primary Latvian enforcement agency for consumer legislation, the Consumer Rights Protection Center (CRPC), is responsible for the supervision and administration of a broad array of financial laws and regulations, including those related to consumer protection, unfair commercial practices and contract terms, consumer credit, distance marketing and advertising. Yet among its 80 staff, the CRPC has no financial sector experts and no specialized unit focusing on financial sector services. At the same time, many important provisions on business (and consumer) conduct regarding financial services are part of the Criminal Code, thereby requiring a higher onus of proof than contraventions of non-criminal legislation¹ and entailing a separate system of enforcement through offices of criminal prosecutors and the criminal courts. Institutions in civil society are also weak, particularly the professional associations and consumer organizations involved in financial services. The court system can be slow while out-of-court mechanisms, such as arbitration courts, lack regulation and procedures to build public confidence. In two areas, banking and insurance, industry-based ombudsmen are, within narrowly defined jurisdictional boundaries, empowered to make non-binding recommendations to the parties to a dispute provided the parties themselves seek such recommendations. For banking, the ombudsman handles only cases related to payments and for insurance, only property and vehicle insurance. While the CRPC received 178 complaints in 2008 and 215 in the first five months of 2009, the two ombudsmen together receive a total of only some 20 to 30 cases a year.

The Diagnostic Review recommends a focus on five key areas. They are: (1) institutional structures, (2) consumer disclosure, (3) business practices of financial institutions, (4) dispute resolution mechanisms and (5) financial education. All five areas are intended to empower consumers by helping them understand the financial contracts they sign and take action when a financial institution appears to have acted contrary to law or the terms of any consumer contract.

The Review presents four approaches to strengthen the institutional framework for financial consumer protection. (1) The CRPC could set up a specialized unit, or at a minimum, hire specialized staff with expertise in financial services. (2) The Financial and Capital Market Commission (FCMC) could play an increased role in financial consumer protection by conducting business conduct supervision in addition to prudential supervision. (3) A specialized financial consumer protection agency could be established. (4) A special agency, such as a financial ombudsman, could be established to handle financial consumer inquiries, complaints and disputes. The approaches are not mutually exclusive. For example, a financial ombudsman could complement the work of CRPC, FCMC or the financial consumer protection agency.

As an initial step, consideration should be given to building up the capacity of CRPC to handle financial sector issues. Although budget cuts are requiring trimming of staff throughout Latvian government agencies, the CRPC should at least designate certain staff to become financial experts. When the current crisis abates, consideration should be given to setting up a special department for financial services. Statistics on financial consumer complaints should be analyzed and published by the CRPC or FCMC so that consumer organizations and professional associations can look for ways to address the common issues that arise for financial consumers. A

¹ The burden of proof in criminal cases is “beyond reasonable doubt” whereas the burden in civil cases is “on the balance of probabilities”.

proper coordinating mechanism between FCMC and CRPC should be put in place to ensure proper exchange of information and mutual education between both agencies.

Financial consumers should be able to receive information that is clear, comprehensible and comparable. For all financial services and products, consumers should be able to obtain information from the providers of financial services in a simple and easy-to-understand format—and one that allows for "comparison shopping" among providers. In Latvia, two banks have announced plans to adopt the European Standardized Information Sheet (ESIS) for pre-contractual information on housing loans. Full implementation of the EU Consumer Credit Directive will further specify what information needs to be provided to consumers. However for any financial service and product, consumers should receive a "Key Facts Statement". This one-page statement should provide a summary of all key terms and conditions for the financial product in question. While obviously not replacing the contract, the Key Facts Statement would provide an easy guide so that consumers would far better understand their financial purchases. Still more important for Latvian consumers would be the adoption of standard contracts or at least standard contractual provisions for basic financial services. The Diagnostic Review found that many contracts for financial services, including consumer and mortgage credit, include provisions commonly found in business-to-business (B2B) contracts and should not be part of business-to-consumer (B2C) contracts. Standardized contract provisions would eliminate this practice. The Review recommends that professional associations develop formats for Key Facts Statements, as well as standardized contract provisions, subject to review and approval by the CRPC or the FCMC.

Business practices for financial institutions should also be improved through codes of conduct. One of the common ways of improving the ways in which financial institutions deal with their retail customers is through the adoption of voluntary codes of conduct, or consumer protection codes. The banking association has already developed a code of conduct, but it is largely unknown to bankers themselves. A consumer protection code could be developed by each professional association for each segment of the financial sector. Alternatively the associations could work with FCMC and CRPC to prepare a single consumer protection code across the financial sector. Regardless of which approach is taken, the consumer protection codes should be placed in bank branches and retail offices of financial institutions and on their websites. Consumers should be advised that if a financial institution fails to follow the code, a complaint can be submitted to the institution, the professional association, or the relevant supervisory agency.

Other measures would also strengthen commercial practices of financial institutions. The professional associations may wish to take on the increased role of providing training and certification for officers who work with retail customers. It would also be helpful if all non-bank credit institutions were licensed (by either the CRPC or FCMC). Regulations are needed for debt collection agencies, which have no specific laws or regulations in place. Also useful would be regulations regarding private credit bureaus, particularly on issues such as retention of data for which no law or regulation currently applies. Debt counseling centers, perhaps through consumer organizations, would also be helpful. Cooling-off periods of 14 days are currently required for financial services and products sold by telephone or over the internet (as per the EU Directive on Distance Marketing). However it would be helpful if cooling-off periods applied to all long-term financial products, such as residential mortgages. (However consumers who decide to cancel contracts during the cooling-off period should be obliged to compensate the financial institution for any loss due to changes in market conditions.)

Dispute resolution mechanisms should also be improved, starting within financial institutions. Most banks designate a department to receive customer complaints but all financial institutions that deal with retail customers should be required to do so—and the contact information for the complaint center should be communicated to consumers. At the same time, the consumer protection codes should include provisions on the maximum number of days (such as 30 days) before a financial institution must respond to a customer complaint.

Over the medium-term, establishing a financial ombudsman may be useful. While the number of financial consumer complaints has doubled in the first six months of 2009, it still remains a small number. A large number of complaints would suggest that consumers have confidence in the government agencies and that they expect to have their complaints regarding financial issues adequately resolved. As the number of complaints grows, further analysis will be needed to separate: (i) inquiries (and requests for information and education); (ii) complaints of "unfair" treatment; and (iii) disputes over contractual issues. A specialized financial ombudsman, as found in the United Kingdom and Ireland, can play a powerful role in dealing with complaints while building public confidence in the provision of financial services. To be effective—and considered independent of financial institutions—a financial ombudsman should be set up by a special law. However such a reform measure would be a long-term program and the costs and benefits would need special review.

Financial education should also be further developed. Latvian primary schools already provide some financial education for students. Such programs are crucial in helping children understand that financial health is as important as physical health. However education and training is also needed for adults. Such training can be provided through professional associations and financial institutions and it should help consumers understand the terms and conditions of the financial contracts they sign. Training for adults should be focused on "teachable moments" such as the time when a consumer becomes a first-time homeowner and signs a mortgage. Planning for retirement is another useful teachable moment. It may also be helpful to conduct "mystery shopping" to see the issues that arise for consumers as they try to buy financial products and learn about the risks and rewards of different products.

A nationwide financial literacy survey would provide a baseline assessment of the current levels of financial capability and serve as an essential means for measuring the impact of consumer protection and financial education programs. Several countries, including the United Kingdom, Ireland, Australia, Canada and Russia, have conducted nation-wide surveys of households assessing not only their levels of financial literacy but also their values and behaviors (taken together called "financial capability"). The survey should be segmented by age, gender, levels of formal education, and geographic area, as well as by rural versus urban areas. Segmentation will provide policy-makers with insight into the key issues for financial consumers as consumers look for ways to meet their debts and plan their financial futures. Such a survey should then be repeated in three to five years, to see if the consumer protection and financial education programs have had the impact that was anticipated—and if the programs should be further modified.

Improvements in five areas—institutional structures, consumer disclosure, business practices, recourse mechanisms and financial education—would substantially strengthen the levels of consumer protection and financial capability in Latvia. The Review recommends that, following discussion of the recommendations, a detailed implementation plan be developed and published.

Introduction

The Diagnostic Review of Consumer Protection and Financial Capability in Latvia is the ninth report in a World Bank-sponsored pilot program to assess consumer protection in financial services in developing and middle-income countries.² The objectives of the Latvia Review are three-fold, namely: (1) to conduct a review of the existing rules and practices in Latvia compared to international good practices regarding consumer protection in financial services; (2) to provide recommendations on ways to improve consumer protection in financial services in Latvia; and (3) to refine a set of good practices prepared by the World Bank for assessing consumer protection in financial services, including financial capability. The Diagnostic Review was conducted at the request of the Consumer Rights Protection Center, with the support of the Ministries of Economics and Finance, as part of the initial stage of a Development Policy Loan under preparation by the World Bank. Valuable input was also provided by ____.

The Good Practices used in the Review are based on international approaches to effective and efficient consumer protection in financial services in both developed and developing countries.³ A set of Good Practices was initially assembled for the Slovakia Review and these Practices have been subsequently revised in the course of further reviews as part of a World Bank pilot program. The Good Practices have been released by the World Bank in the form of a Consultative Draft in order to receive feedback and comment from international regulators, supervisors and other stakeholders. The Good Practices incorporate the provisions of the EU Directives related to consumer protection and the reports of European financial regulatory and supervisory agencies, as well as laws, regulations and business practice codes in the United States, Australia, Canada and other countries. The United Nations Guidelines for Consumer Protection have also been useful references regarding general consumer protection. The Organization for Economic Cooperation and Development (OECD) has also released sets of good practices to enhance education and awareness on risk and insurance, pensions, and credit products⁴, supplementing the recommendations presented in its 2005 global review of financial education programs.⁵ The Diagnostic Review for Latvia affords the first opportunity to test the Good Practices in a country in the midst of financial crisis.

The publication of the Diagnostic Review for Latvia aims to enhance development of financial consumer protection both in Latvia and worldwide. In particular, it is anticipated that application of the Good Practices in middle-income countries, such as Latvia, will contribute to international policy dialogue regarding the key components of financial consumer protection and will assist in the development of benchmarks that are widely accepted as generally applicable to consumer protection in financial services in any jurisdiction.

² In chronological order, other reports on consumer protection in financial services have been prepared for the Czech Republic, Slovakia, Azerbaijan, Romania, Croatia, Russia, Lithuania and Bulgaria. The published final reports can be downloaded at <http://www.worldbank.org/eca/consumerprotection>.

³ The World Bank has released the document *Good Practices for Consumer Protection and Financial Literacy in Europe and Central Asia: A Diagnostic Tool* as a Consultative Draft. A copy can be downloaded at <http://www.worldbank.org/eca/consumerprotection>.

⁴ See OECD, *Improving Financial Education and Awareness on Insurance and Private Pensions* (2008) available at http://www.oecd.org/document/8/0,3343,en_2649_34851_41210376_1_1_1_1,00.html. OECD, *Recommendation on Good Practices on Financial Education and Awareness Relating to Credit* (2009) at http://www.oecd.org/document/39/0,3343,en_2649_15251491_43269479_1_1_1_1,00.html

⁵ See OECD, *Improving Financial Literacy: Analysis of Issues and Policies* (2005), available at http://www.oecd.org/document/28/0,3343,en_2649_15251491_35802524_1_1_1_1,00.html

The Review is presented in two volumes. Volume I notes the importance of consumer protection in financial services, describes the Government's policy strategy for financial consumer protection, provides statistics on the size and growth of the retail financial sector in Latvia, and sets out the key findings and recommendations of the Review. Volume II provides an assessment of the Latvian consumer protection institutional and legal framework and practices against the benchmark of Good Practices for six segments of the financial sector—banking, non-banking credit institutions, securities, insurance, private pensions and credit reporting systems.

Importance of Consumer Protection & Financial Capability

At its heart, the need for consumer protection arises from *an imbalance of power, information and resources between consumers and their financial service providers, placing consumers at a disadvantage.* Consumer protection aims to address this market failure. Financial institutions know their services well but individual retail consumers may find it difficult or costly to obtain sufficient information on their financial purchases. Personal insurance, such as auto or life insurance, are often cited as examples of the imbalances. The complex contracts prepared by insurers—and the risk allocation between the consumer and the financial institution—are often beyond the capacity of most consumers to understand. Particularly in the post-transition countries of Europe and Central Asia, the public lacks a history of using sophisticated financial services. Even highly literate and well-educated consumers often have no experience among their friends and extended family of negotiating a complex financial service, such as mortgage for a house purchase.

Strong financial consumer protection helps build public trust in financial institutions. The trust of consumers in their financial service providers is critical for the long-term development of the financial sector. To build that trust, an effective and efficient consumer protection framework should provide consumers with:

- ***Transparency*** by providing full, plain, adequate and comparable information about the prices, terms and conditions (and inherent risks) of financial products and services;
- ***Choice*** by ensuring fair, non-coercive and reasonable practices in the selling of financial products and services and collection of payments;
- ***Redress*** by providing inexpensive and speedy mechanisms to address complaints and resolve disputes;
- ***Privacy*** by ensuring control over access to personal financial information; and
- ***Access to financial education*** that enables consumers develop the financial capability required to understand the risk/return (cost/benefit) trade-offs, and their rights and obligations regarding the financial products and services that they buy.⁶

However regulation also imposes a cost on the financial sector. Regulation can impair both competition and innovation in the financial sector, thus raise consumer costs and obstruct development of adequate market discipline that would hold risk-taking in check. Clear priorities need to be set. Regulation should be subject to cost-benefit analysis and consumer protection regulations should be assessed to determine their impact on sound consumer finance.

⁶ Financial education is also needed to help households in making long-term financial decisions, such as savings for retirement or sending children to college. However such "life-cycle" planning is beyond the direct scope of consumer protection in financial services.

The global financial crisis has highlighted weaknesses in consumer protection and financial capability—and their impact on global financial institutions. In its April 2008 report, the Joint Forum of the Basel Committee on Banking Supervision, the International Organization of Securities Commission and the International Association of Insurance Supervisors identified three key risks related to possible "mis-selling" of financial products to retail customers.⁷ These were: (1) legal risk, if successful lawsuits from collective (i.e. class) action by customers or enforcement actions by supervisory agencies result in obligations to pay financial compensation or fines; (2) short-term liquidity risk and long-term solvency risk, if retail customers are treated unfairly and thus shun the financial institution and withdraw their business; and (3) contagion risk, if the problems of one financial institution (or type of financial product) spread across the financial sector. Effective consumer protection can help ensure that the actions of financial firms do not make them subject to criticisms of mis-selling.

Consumer protection could also shield the financial sector from the risk of political over-reaction in periods of financial turmoil. The political response to collapses of parts of the financial sector may be to over-compensate with heavy regulation. The impact of too little consumer protection became evident, for example, during the insurance and superannuation scandals in the United Kingdom and Australia. As a result of the scandals, extensive studies were conducted recommending wide-ranging regulatory reforms. In addition, some countries have resorted to interest rate caps with questionable results, especially on the development of the credit market.

Latvian Policy for Financial Consumer Protection in the EU Context

The EU Consumer Policy strategy 2007-2013 aims to strengthen consumer protection and financial capability.⁸ The strategy has three objectives, namely: (1) to empower consumers by ensuring that they have real choices, accurate information, market transparency, and the confidence that comes from effective protection and solid rights; (2) to enhance consumers' welfare regarding price, choice, quality, diversity, affordability and safety of products; and (3) to protect consumers as a group from the serious risks and threats that cannot be withstood on an individual basis. Key steps for the implementation of the strategy involve development of benchmarks for national consumer policies, including a consumer protection policy for the financial sector, and collection of service quality data and complaint statistics. The EU takes the approach that an effective regime of financial consumer protection covers three areas. Consumers should have access to: (1) sufficient information to make informed decisions in the purchase of financial services, (2) cost-effective recourse mechanisms to redress violations of financial service contracts, and (3) programs of financial education.

In addition, the EU is engaged in an extensive program to further strengthen consumer protection in financial services. Annex 1 provides a listing of the key EU Directives related to financial consumer protection and their transposition into Latvian law. In 2008, the European Parliament approved the revised Consumer Credit Directive, which requires a substantially increased level of disclosure of the terms and conditions of consumer credits. (Transposition of

⁷ Joint Forum of the Basel Committee on Banking Supervision, the International Organization of Securities Commission and the International Association of Insurance Supervisors, *Customer suitability in the retail sale of financial products and services*, April 2008.

⁸ EU Consumer Policy Strategy 2007-2013 COM (2007) 99 final.
http://ec.europa.eu/consumers/overview/cons_policy/EN%2099.pdf.

the Directive is required before 2010. Latvia has prepared draft legislation to incorporate the revisions.) However as the European Commission (EC) has pointed out, most consumer protection directives require only "minimum harmonization." As a result, EU Member States have often expanded the laws and regulations related to consumer protection. To provide a common framework, the Commission has proposed a new Consumer Rights Directive that would supersede existing Directives on Unfair Contract Terms, Distance Selling, and Doorstep Selling. (Another Directive—on Sale of Consumer Goods and Guarantees—would also be included but this does not relate to financial services.)⁹

Financial education is also being emphasized in the program under development in the EU.

In November 2007, the EC released its survey of over 150 financial education programs conducted in the 27 EU Member States. An October 2008 report of the European Parliament identified measures to be taken to improve financial education throughout the EU.¹⁰ In its *Communication on Financial Education* the EC noted it would conduct a comprehensive review in 2010 to evaluate the effectiveness of existing programs of financial education among EU Member States.¹¹

The Latvian Consumer Protection and Market Surveillance Program follows the EU approach. The Program which covers the years 2008-2010, aims to ensure higher levels of consumer protection in Latvia, by incorporating enhanced consumer protection into laws, regulations and government policies and by more fully engaging civil society in consumer protection issues. The strategy covers consumer protection throughout all economic sectors, including financial services. The current program focuses on five areas:

- 1) Improving the legal basis for consumer rights protection;
- 2) Creating an enabling business environment by appropriate and effective market surveillance and enforcement of consumer rights protection laws;
- 3) Informing consumers and businesses about consumer protection issues and encouraging consumer education;
- 4) Improving alternative dispute resolution procedures at domestic and cross-border levels; and
- 5) Strengthening performance of non-governmental consumer organizations.

The October 2008 Eurobarometer survey of the 27 EU Member States suggests that Latvian consumers would welcome a strengthened consumer protection framework for all sectors, including those that provide financial services. The Eurobarometer survey was requested by DG SANCO to look at consumer protection in all sectors (including financial services).¹² Among the 27 EU Member States, Latvia had the fourth highest percentage of population concerned that consumer protection remained too weak. More than half of Latvian consumers (54 percent) thought they were inadequately protected by existing general consumer protection measures while among the EU just 39 percent were similarly concerned.

⁹ See http://ec.europa.eu/consumers/rights/cons_acquis_en.htm

¹⁰ European Parliament, *Report on protecting the consumer: improving consumer education and awareness of credit and finance* (2007/2288(INI)), October 2008.
<http://www.europarl.europa.eu/sides/getDoc.do?language=EN&reference=A6-0393/2008>.

¹¹ European Commission, *Communication from the Commission: Financial Education*, COM (2007) 808 final <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52007DC0808:EN:NOT>.

¹² European Commission, Special Eurobarometer No. 298, *Consumer protection in the internal market*, October 2008.

Regarding general consumer protection in goods and services, Latvian consumers are primarily interested in having strong laws to protect their interests. When asked how best to protect consumers, the Eurobarometer survey found that the largest number of Latvian consumers (49 percent) chose the legal right to terminate a contract or ask for a price reduction. The next best way to protect consumers was the legal right to return a product or cancel a service within the cooling-off period (for 34 percent of Latvians), followed by the legal obligation of providers to ensure safe goods and services (31 percent). The third choice was disclosure. Fewer than one-third (30 percent) thought that clear written information about the goods or services and the sales contract was the best way to protect consumers. While the Eurobarometer survey provides useful insights, a survey focused exclusively on protection in respect of financial services rendered to Latvian consumers would be helpful.

Private sector surveys show that Latvian consumers have low levels of confidence in their ability to make sound consumer finance decisions. A survey covering 1,007 respondents throughout Latvia, was commissioned by GE Money in February 2006 and conducted by Latvian Facts, a market research agency based in Riga, in order to study public attitudes and experiences regarding consumer credit. The survey found that 46 percent of Latvians were concerned that they lacked adequate knowledge relating consumer credit issues. At the same time, only about one-third (37 percent) were familiar with available dispute settlement options.

Background on Latvian Household Finances

Latvian households have become increasingly indebted with exposure to currency and interest rate risks. Household loans have more than tripled over the last four years. Most loans are to finance house purchases. Households have increasingly borrowed in Euros and other foreign currencies to finance their needs. By June 2009, over 88 percent of total household loans were denominated in foreign currencies (see Table 1). Most housing loans were also at variable rates of interest, exposing Latvian consumers to changes in not only foreign exchange rates, but also interest rates.

Table 1: Household Loans
(balances in LVL million)

	Dec-05	Dec-06	Dec-07	Dec-08	Jun-09
Loans for House Purchases	1,749.7	3,260.6	4,710.4	5,054.5	4,953.6
<i>as % of GDP</i>	19.31	29.19	31.87	31.12	33.01
Consumer Credit	363.0	593.5	721.0	793.1	764.4
<i>as % of GDP</i>	4.01	5.31	4.88	4.88	5.09
Other Loans	339.0	449.1	557.4	554.8	539.1
<i>as % of GDP</i>	3.74	4.02	3.77	3.42	3.59
Total Household Loans	2,451.7	4,303.2	5,988.8	6,402.4	6,257.1
<i>of which foreign currency loans</i>	69.7%	77.1%	85.8%	87.4%	88.5%

Source: FCMC, Central Statistical Bureau

Mortgages are used to collateralize not only house purchases but also consumer credit. While over 99 percent of loans for house purchases were collateralized by residential mortgages, more than 60 percent of consumer credits used home mortgages to secure their loans. Consumer

credit also relied on sureties from co-signers (for 6 percent of credits) and other collaterals. However over 25 percent of consumer credits were granted with no collateral at all (see Table 2).

Table 2: Structure of Collaterals for Household Loans
(in percentage)

	Consumer Credit	House Purchase	Payment Cards	Other	Total
Mortgage	60.97	99.24	4.81	79.16	90.22
Sureties	5.93	0.37	0.11	7.25	1.34
Cash Deposits	0.19	0.09	0.53	6.27	0.63
Securities	0.06	0.00	0.37	2.55	0.23
Commercial Pledges	2.10	0.00	0.00	0.78	0.22
Other Collaterals	5.23	0.00	0.02	0.19	0.41
No Collateral	25.52	0.29	94.14	3.80	6.95
Total	100.00	100.00	100.00	100.00	100.00

Source: FCMC, *Banking Activities in 2nd Quarter of 2009*
Date of Data: June 2009

At the same time, housing collateral has been heavily leveraged. For residential mortgages, Loan-to-Value (LTV) ratios have been rapidly increasing in recent years (see Table 3). Such high levels of LTV suggest that inadequate attention has been paid to underwriting practices and policies by housing lenders.

Table 3: Structure of Housing Loans Loan-to-Value Ratios
(in percentage)

	Jun-06	Dec-06	Jun-07	Dec-07	Jun-08	Dec-08	Jun-09
LTV <70%	61.52	55.62	50.21	50.19	50.31	51.63	54.10
LTV 70-100%	35.10	40.60	46.26	45.96	45.51	45.50	42.16
LTV >100%	3.38	3.78	3.54	3.84	4.18	2.87	3.74
Total Housing Loans	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Source: FCMC

The result has been heavily indebted households. By the end of 2007, mortgage debt in Latvia represented 31 percent of GDP. Among the new EU Member States at 1 January 2008, Latvia had the second highest ratio of mortgage debt to GDP, second only to Estonia (see Table 4). Swedbank estimates that 20 percent of Latvian residents have taken mortgage loans¹³ and the 2006 GE Money Survey suggested that as many as one third of Latvians had taken consumer loans. The GE Money Survey also found that the largest percentage of borrowers were those aged 25-39, with higher levels of education higher income levels and at least one child under the age of 15.

¹³ *Baltic Business News*

Table 4: Mortgage Debt to GDP

	Mortgage Debt / GDP (%)
Estonia	32.7
Latvia	31.0
Lithuania	19.2
Croatia	15.3
Hungary	11.4
Poland	8.3
Ukraine	7.1
Bulgaria	7.0
Kazakhstan	5.3
Russia	2.0

Note: Data as of December 2007, except for Lithuania (October 2008) and Latvia (December 2008)
Source: Various sources compiled by World Bank

As early as 2005, Latvia had one of the highest percentages in Europe of households with arrears on bills. According to data of EU SILC 2005, 23 percent of Latvian households were in arrears in the previous 12 months on mortgage, rent, utility bills, hire-purchase or loan payments. This percentage was the second highest among the EU Member States in the same 2004 to 2005 time-frame, second only to Greece. Over one-third (37 percent) of these Latvian borrowers complained at the same time that the costs of credit or housing represented a “heavy burden” on their lives.¹⁴

Table 5: Average Annual Expenditure in Financial Services per Household Member
(as percentage of total expenditure)

	2003	2004	2005	2006	2007	2008
Insurance	0.83	1.06	1.01	1.16	1.28	1.44
Motor third party liability	0.37	0.40	0.40	0.37	0.40	0.49
Auto insurance	0.14	0.21	0.18	0.29	0.46	0.47
Health insurance	0.21	0.35	0.32	0.35	0.28	0.29
House insurance	0.11	0.10	0.10	0.14	0.14	0.17
Financial services and fees	0.23	0.29	0.26	0.20	0.19	0.20
Financial services	0.14	0.17	0.18	0.15	0.12	0.14
Fees	0.09	0.12	0.08	0.05	0.06	0.06
All Financial Services	1.05	1.34	1.27	1.36	1.47	1.64

Source: Central Statistical Bureau

The high level of household debt (as well as foreign exchange and interest rates exposures) places strains on the Latvian financial sector. By June 2009, non-performing loans in the household sector reached 5 percent of GDP.

¹⁴ European Commission, *Towards a Common Operational European Definition of Over-indebtedness*, February 2008

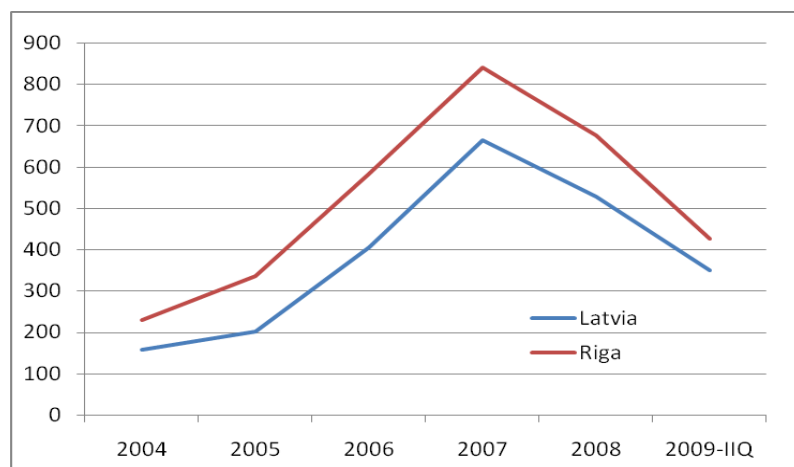
Table 6: Non-performing Loans
(as percentage of GDP)

	Dec-05	Dec-06	Dec-07	Dec-08	Jun-09
Total Household Loans	0.38	0.16	0.40	2.05	5.17
Housing purchases	0.29	0.07	0.23	1.47	3.82
Consumer credit	0.05	0.04	0.06	0.16	0.46
Other loans	0.04	0.04	0.11	0.42	0.90

Source: FCMC, Central Statistical Bureau

Rapid change in Latvian housing prices has compounded the problem. According to the Central Statistical Bureau, the average price of urban houses in Latvia had been rapidly increasing in 2006 and 2007. The annual increase of urban housing prices for 2006 was 100 percent in Latvia and 74 percent in Riga. By the end of 2007 the average urban housing price per square meter reached LVL 665 in Latvia and LVL 841 in Riga. However in 2008 house prices fell about 20 percent. By June 2009 urban housing prices have decreased almost 50 percent relative to the levels of 2007.

Figure 1: Average Urban Housing Prices in Latvia
(in LVLs per square meter)



Source: Central Statistical Bureau

Financial assets of Latvian households are highly liquid but cover only half of household debt. About 80 percent of household financial assets is held as bank deposits (see Table 7). Another 15 percent is held as private pension funds (i.e. the Pillar II occupational pension funds requiring mandatory participation for workers.) While non-life insurance has grown, policies sold to households remain small at less than 1 percent of GDP. Household investments in securities and investment funds are largely non-existent, with securities investments made through the pension funds. Taken in aggregate, household financial assets represented only 55 percent of household borrowings at the end of 2008. This provides Latvian households with little margin to cover the risk of increased loan payments due to a rising interest rate or a falling foreign exchange rate or both.

Table 7: Household Financial Assets
(in LVL thousand)

	Dec-05	Dec-06	Dec-07	Dec-08	Mar-09
Bank Deposits	1,819	2,638	3,036	2,883	2,824
as % of GDP	20.1%	23.6%	20.5%	17.7%	17.9%
Non-life Insurance *	51	63	96	124	123
as % of GDP	0.6%	0.6%	0.7%	0.8%	0.8%
Life Insurance	11	16	26	19	19
as % of GDP	0.1%	0.1%	0.2%	0.1%	0.1%
Pension Funds - Pillar II	82	122	240	464	553
as % of GDP	0.9%	1.1%	1.6%	2.9%	3.5%
Pension Funds - Pillar III	36	513	65	74	73
as % of GDP	0.4%	0.5%	0.4%	0.5%	0.5%
Total Household Financial Assets	1,999	2,890	3,463	3,565	3,593

* Includes motor third-party liability, personal accident and health insurance.
Data of household assets in securities is not available.
Source: FCMC, Central Statistical Bureau

At the same time, not all Latvians use formal financial services.¹⁵ It is estimated that only 64 percent of Latvians have an account with any financial intermediary. This is lower than Lithuania (70 percent) and Estonia (86 percent) as well as the average of western European states (91 percent). Despite the widespread increase in the use of financial services in Latvia, one third of the population still does not access the formal financial sector.

Table 8: Access to Financial Services

	% of Population
Slovenia	97
Estonia	86
Slovakia	83
Lithuania	70
Russian Federation	69
Hungary	66
Poland	66
Latvia	64
Bulgaria	56
Kazakhstan	48
Croatia	42
Ukraine	24
Romania	23
Average Western Europe	91

Note: Data as of December 2007
Source: World Bank

¹⁵ World Bank, *Finance for All? Policies and Pitfalls in Expanding Access*, 2008.

Key Findings & Recommendations

While Latvia has adopted the required EU Directives, the institutional structures have had difficulty in addressing the issues facing financial consumers. Throughout the new EU Member States, finding ways to build the necessary institutional structures—both in the government and civil society—has proven to be a challenge. The new institutions need not only clear legal authority but also resources and staff able to fulfill the mandates set by law or government policy.

The Review recommends consideration of five key areas of reform. They are:

- 1) Strengthening the institutions responsible for financial consumer protection,
- 2) Improving consumer disclosure for all financial services,
- 3) Improving the business practices of financial institutions when dealing with their retail customers,
- 4) Expanding the dispute resolution mechanisms for financial consumers, and
- 5) Expanding programs of financial education and financial capability for both students and adults.

Institutional Structures

The Latvian government agencies have broad legal authority to protect the rights and interests of financial consumers.¹⁶ As part of the Law on the Financial and Capital Market Commission (FCMC), the goals of the FCMC are to protect the interests of investors, depositors and insured parties and promote the development and stability of the financial and capital market. However the Consumer Rights Protection Center (CRPC) has a still broader responsibility for consumer protection. While the CRPC is responsible for the enforcement of over 90 laws and regulations, three laws and one regulation are particularly important, namely the Consumer Rights Protection Law, the Unfair Commercial Practices Prohibition Law, as well as the Cabinet of Ministers Regulation regarding Consumer Credit Agreements.

By the terms of the Consumer Rights Protection Law, the CRPC ensures the effective protection of consumer rights and interests, including those of consumers of financial services. Consumer rights are violated if contract terms are "unfair," for example if the terms have been unilaterally changed by the service provider. Under the Law, supervision and control of consumer rights protection is to be implemented primarily by the CRPC with the assistance of other authorized State institutions, in cooperation with local governments and consumer associations. At the same time, CRPC is the monitoring institution for the Unfair Commercial Practices Prohibition Law¹⁷, which prohibits commercial institutions from using unfair business-to-consumer (B2C) practices. The legislation states that commercial practices are considered unfair if they meet any of several criteria: (1) do not conform with professional diligence or could negatively impact the economic behavior of an *average* consumer or (2) are misleading or aggressive.

¹⁶ The Consumer Rights Protection Law defines a "consumer" as a natural person who expresses a wish to purchase goods or utilize services for a purpose, which is not related to his or her economic or professional activity. This would exclude microfinance entrepreneurs and others intending to use consumer services to gain profit.

¹⁷ Along with the Health Inspectorate for medical products and the Food and Veterinary Service for veterinary medical products.

The legislation provides specific tools to the CRPC in its role to protect consumers. Under the Consumer Rights Protection Law, the role of the CRPC includes: (1) monitoring and controlling service providers and (2) examining consumer complaints and requiring that institutions comply with lawful claims. To implement this role, the CRPC has the right to take decisions that require service providers to cease violations and rectify the impact on consumers, publish the CRPC's decisions in whole or in part in the official gazette (*Latvijas Vestnesis*), and apply sanctions as per the Administrative Violations Code. Currently the maximum institutional fine under this Law is LVL 10,000 (or about USD 20,000) which is not sufficient to deter illegal behavior by financial institutions.

The CRPC is responsible for enforcing consumer protection in all spheres of the economy including the provision of financial services—but lacks technical expertise in financial sector issues. The CRPC has a broad mandate that includes special projects for monitoring personal protection equipment, children's toys, electrical products, building materials, wheels for off-road vehicles as well as financial consumer services. While the CRPC staff of about 80 officials has extensive expertise in tangible product consumer protection issues and the applicable legislation, no staff member has expertise in respect of financial services. Furthermore, it is difficult for any single agency to cover such a broad array of products, particularly since the regulation of financial services requires a particularly high level of specialized expertise. In addition, such expertise is expensive for government agencies to develop since financial sector experts often find themselves in demand in the private sector.

Four approaches are available to strengthen the institutional framework for financial consumer protection. (1) The CRPC could set up a specialized unit, or at a minimum, hire specialized staff with expertise in financial services. (2) The FCMC could play an increased role in financial consumer protection by conducting business conduct supervision in addition to prudential supervision. (3) A specialized financial consumer protection agency could be established. (4) A special agency, such as a financial ombudsman, could be established to handle financial consumer inquiries, complaints and disputes. The approaches are not mutually exclusive. For example, a financial ombudsman could complement the work of CRPC, FCMC or the financial consumer protection agency.

Each approach has its advantages and disadvantages. None of the choices is attractive, however, in an environment where the Government is cutting its administrative budget by 30 percent or more and focusing on improving the efficiency of public administration. However maintaining the status quo would leave the CRPC stretched in its ability to monitor the financial services markets and deal with an increasing number of financial consumer complaints.

Each approach should be carefully considered. The *first* approach—setting up a special financial services unit within CRPC—will likely require additional budget funding to expand staff and provide the necessary training. In some countries, financial supervisory agencies have seconded staff to the consumer protection agency to help build the necessary expertise within the consumer agency. For this, technical assistance from other EU Member States may be helpful. The *second* approach—expanding the supervisory role of the FCMC to include consumer protection—would require that FCMC provide not only prudential supervision over financial institutions but also supervision of business conduct. Many financial supervisory agencies in Europe, such as in the United Kingdom, Ireland, and the Czech Republic, have chosen this option as the most efficient. Conflicts of interest between prudential and business conduct supervision inevitably arise. However the agencies have found that putting the two roles together provides valuable information—and early warning—for the purpose of financial services supervision. The *third* approach, namely a separate financial consumer protection agency, is the most difficult but

is already in place in Canada and has recently been proposed by the Obama administration for the United States. The *fourth* approach, namely the establishment of a financial services ombudsman, separates the complaints handling and dispute resolution process from market surveillance and policy-development. Offices of financial ombudsmen have proven to be successful means to address complaints and build public confidence in the financial sector in the United Kingdom and Ireland, and such an office is being considered for Italy.

The starting point should be building up the capacity of the CRPC to handle financial sector issues, with support from the FCMC. The Review recommends that as an initial step, consideration be given to the first option—building the CRPC's expertise in financial services. In this case, the FCMC should provide technical support to the CRPC. Additional assistance could be provided through twinning arrangements with authorities from other EU countries. However if building financial sector expertise of the CRPC is not possible—due to budget or other constraints—FCMC should be obliged to expand its role to include consumer protection, in addition to prudential supervision. In this scenario, the FCMC should face intense accountability for the balance of its work, to make sure that it deals with both functions properly. In any case, a proper coordinating mechanism between FCMC and CRPC should be put in place to ensure proper exchange of information and mutual education between both agencies. FCMC should focus on improving the understanding of the financial sector by the CRPC staff, while CRPC should focus on explaining the importance of consumer protection alongside prudential supervision to secure a functioning and stable financial sector.

The legislation provides for an active role for consumer associations. The Consumer Rights Protection Law provides for consumer associations to play an active role including: (1) participating in inspections together with the CRPC to review the quality of consumer services, (2) examining complaints and proposals of consumers, (3) representing consumers in court and (4) submitting proposals to the CRPC on ways of addressing specific violations of the Consumer Rights Protection Law. However in practice, consumer associations fail to assist consumers adequately and, in financial services, they play no role at all. Not only do these associations lack funding, their institutional structures are less than ideal. PIAA (the Latvian National Association for Consumer Protection) acts as an umbrella consumer organization and includes some 10 consumer associations (or clubs) and tenant organizations. Club for Protection of Consumer Interests is the oldest consumer club in Riga with 18 years of operation. The second oldest is the Consumer Support Centre, with 15 years of operation. However no consumer association has expertise in financial services. The associations have limited access to funds and only in 2007 the CRPC provided funding to them (about LVL 30,000). In addition, consumer associations have the right to participate in the Consultative Council, an advisory body to the CRPC on consumer protection issues, set up in 2006. However, the several meetings of the Consultative Council have yet to be effective in advising on measures to strengthen consumer protection in financial services. An alternative would be to set up a consultative board for financial services within the CRPC, with participation of experts from the FCMC, industry associations and consumer organizations.

Nevertheless, consumer associations should be strengthened. Once the current budget crisis is over, the Ministry of Economics may wish again to consider providing some project funding for the consumer associations to help financial consumers. This is the approach taken by Slovakia, for example, which provides a total of Euros 2 million for consumer associations. Another approach would be to allow consumer associations to generate their own funds. In Russia, for example, where the Confederation of Consumer Associations (KonfOP) litigates cases on behalf of consumers, KonfOP is permitted to retain one-half of court-awarded damages compensation. A similar approach might be effective in Latvia. However, as early as possible, measures should be

taken to improve the effectiveness of the Consultative Council or an alternative consultative board on financial services. The body should have specific terms of reference that are placed on the CRPC's website and develop recommendations and advice for the CRPC, based upon financial service complaint statistics and other measurements of consumer sentiment regarding the provision of financial services.

At the same time, the authority of the FCMC should be strengthened to deal with unregistered firms. Any legal entity that accepts funds from the public should be subject to public oversight. This is required under Latvian law. However for unregistered firms, only the police authorities have responsibility to halt their activity and the FCMC has no authority to take action or to cause them to cease their activities. The problem is that police generally lack the expertise to deal with financial firms, who when stealing from the public leave no trace of a physical crime. In the interests of protecting investors, the FCMC should have the legal authority to take action against unregistered firms. Also on the FCMC's website, a webpage of consumer alerts should notify the public about the activities of unregistered financial firms. In addition, the FCMC is limited (as is the CRPC) by the maximum fine of LVL 10,000 (or USD 20,000) set up by the Administrative Violations Code. The FCMC should be able to impose large fines when necessary to curb illegal behavior by financial firms.

Consumer Disclosure

At the foundation of effective financial consumer protection is consumer disclosure. Financial institutions should be obliged to present their financial products in a clear and comparable format, which is easy for consumers to understand and allows consumers to compare offers from different financial institutions. Where consumers can obtain clear and comparable information, they can make informed choices and ensure that the financial products that they purchase are suitable for their needs and objectives. They can also compare other products from different financial service providers so as to find the best one to meet their needs. The 2008 Eurobarometer Survey also noted that thirty percent of Latvian consumers think that disclosure is an important right related to consumer protection. Clear laws and regulations—and effective enforcement mechanisms—are needed to ensure meaningful disclosure of consumer financial products. At the same time, Latvian consumers tend not to complain about their credit agreements. In the GE Survey, over half (55 percent) thought that their agreements were not overly complicated or difficult to understand and 72 percent considered that the information they received was sufficient. In spite of contracts that appear to be easy to understand, a common complaint received by the authorities is that consumers did not eventually understand the terms and conditions of the financial service contracts they signed. For all regulations regarding consumer disclosure, the authorities should make sure that the public clearly understands the disclosed information and knows how to use it to make informed decisions. Consumer testing of proposed disclosure rules or formats would be helpful.

Latvian regulations provide some requirements on calculation and disclosure of consumer credits but this is not sufficient. The August 2008 Regulation 692 of the Cabinet of Ministers specifies the details of the calculation of the interest rate for consumer credits and how the consumer credit shall be advertised, including among other requirements the disclosure of the effective interest rate. Transposition of the EU Directive on Consumer Credit into Latvian law (as is currently under preparation) will require disclosure of the Annual Percentage Rate of Charge (APR) and other key terms for borrowers of consumer credits but no laws or regulations provide

detailed direction on disclosure for other types of consumer financial services (including mortgage loans).

A standardized Key Facts Statement for each type of standard retail financial service would help consumers understand the key conditions of their contracts. For financial services, consumers need a short standardized description written in plain language that is comparable across products provided by different institutions. For mortgages, two banks (*SEB Banka* and a smaller bank, *Rietumu Banka*) have announced plans to adopt the European Standardized Information Sheet (ESIS) to provide pre-contractual information for home loans. However a Key Facts Statement for each type of retail financial service would provide such standardized information for consumers. The format for key facts disclosure should allow consumers to easily and quickly identify the key terms and conditions of financial contracts. Requiring that all financial institutions prepare their offers for commonly-used retail financial services in a standardized format will further facilitate the ability of consumers to shop around and compare offers—and thus ultimately increase transparency and competition in the financial sector.

For consumer credits, ten different areas should be covered. The Key Facts Statement should summarize in a page or two all key terms and conditions of the specific product or service being provided. This would include (1) the APR, (2) the total amount of the credit, (3) the amounts of monthly payments, (4) the final maturity of the credit or investment, (5) the total amount of payments to be made, (6) all fees—particularly prepayment and overdue penalty fees—and any other charges that could be incurred, (7) any required deposits or advance payments, (8) if the interest rate is variable, the basis on which the calculation is made and a published source (such as a newspaper) where the consumer can verify the base rate, (9) if any additional insurance (such as personal mortgage insurance) is required to maintain the credit and, if so, the nature and extent of necessary coverage, and (10) the name of the department (with telephone number, fax number and email address) where inquiries, complaints and disputes can be submitted to the financial institution. If the credit is being provided by a retailer to finance a consumer product, such as a television or washing machine, the consumer should also be advised of the cash price of the product without financing charges. Special attention should be paid to credit card disclosures, where consumers need to be clearly informed of the financial impact on them of paying only the minimum amount due. For the credit reporting system, a brochure could explain to consumers the procedures for correcting inaccurate information in the credit registers. The Key Facts Statements would obviously not replace the contract for legal purposes but each financial institution would be obliged to ensure that their Key Facts Statements included no incorrect or materially misleading information. The implementation of the EU Directive on Consumer Credit would require the introduction of the Standardized European Consumer Credit Information format. This would be an important first measure to implement a key facts disclosure requirement for credit products.

Special risks should also be disclosed to consumers. For any credit secured by real property (such as a house or apartment), the mandatory disclosure should note that in the case of default, the lender could ultimately seize and sell the property. In addition, for loans denominated in a foreign currency (such as Euros), the mandatory key facts disclosure should contain a warning that changes in exchange rates could increase the total amount of debt. The Key Facts Statement should also note that, for variable interest-rate loans, the interest rate could vary, depending on the level of the underlying base rate.

Additional specialized disclosure should be required for investment services. For any investment service, the consumer should also be advised of the percentage commission charged for each service. Regulations should be issued to set out in detail the disclosure requirements for

prospectuses and simplified prospectuses of mutual funds, especially for calculating the net asset value of real-estate funds. Regulations should also standardize the account opening disclosures for brokerage accounts and collective investment funds.

Consumer disclosure for insurance products should be strengthened. The insurance legislation should require mandatory disclosure of commissions payable to intermediaries in relation to single premium investment products. The legislation should also be revised to ensure that where consumers are required by merchants or credit providers to insure with a particular company adequate disclosure is made to the consumer. The disclosure should include the relationship between the credit provider or merchant and the selected insurance provider, the benefits which the merchant or credit provider will derive from the arrangement and a comparison of the costs to the consumer with the costs of a number of other alternatives.

Consumer disclosure for private pensions should be improved. At a minimum, the investment returns should be presented on a risk-adjusted basis, identifying the basic risk parameters, such as the estimate of one standard deviation as a measure of the volatility of the pension fund, among other parameters. Importantly, consumers need to be informed that investment returns in the pension funds are not guaranteed and that participants could lose their principal at any time.

It is recommended that the standard formats for Key Facts Statements be developed by the professional associations. The supervisory agencies should also review and comment on the formats (for example, to ensure that they provide material information that would not mislead consumers) but the preparation of the formats would best be done by the respective professional associations. Thus, for consumer credits, the Association of Latvian Commercial Banks would develop a standard format that would allow banks to efficiently prepare the Key Facts Statements, which would be reviewed by the FCMC and the CRPC. Non-bank credit providers might also comment on the format, although to date no professional association of consumer finance companies or other form of non-bank credit institutions has been put in place. For house purchase loans, the Association of Latvian Commercial Banks should adopt the ESIS. It is also recommended that the professional associations for insurance companies and pension management companies prepare Key Facts Statements for their standard retail financial services—and their formats should be reviewed by the FCMC. The Key Facts Statements should also be tested in order to ensure that the average consumer understands their content and can use the information to make relevant comparisons and decisions. The professional associations for each type of financial service should formally adopt the format of the Key Facts Statements and encourage their member institutions to use the Key Facts format. In addition, at the time of onsite supervision, the FCMC should review the pre-contractual information provided by financial institutions to their retail customers.

Tariff surveys showing comparison of prices of financial services would also be helpful. Surveys of offered prices for standardized services could be conducted by the professional associations or consumer associations or the CRPC. However, it would be best if the surveys are conducted by the CRPC to make sure that the surveys are independent and not influenced by sponsorship, and that they will be conducted regularly (so that a long-term database can be built). Alternatively, the associations or the financial supervisors or the CRPC could set a format for disclosure and the financial institutions could provide the data to the public. In Ireland, for example, tariff surveys conducted by the Financial Regulator have proved to be an effective mechanism for encouraging consumers to engage in "comparison shopping" before purchasing a financial service.

Consideration should be given to the use of standard contracts, or at least the use of standard clauses in contracts for consumer financial services. A review of the financial complaints submitted to the CRPC shows that most relate to the terms of contracts, which include provisions commonly seen in business-to-business (B2B) contracts rather than in business-to-consumer (B2C) contracts. One example is a residential mortgage contract which requires additional collateral if the value of the property falls by more than a minimum percentage. Another example is a loan for housing purchase where the borrower is obliged to provide additional credit risk information in cases where property prices have fallen. Providing additional collateral or credit information is common in B2B transactions, or in the case of investments by sophisticated investors. However, they are not typically seen for consumer finance transactions at least in other jurisdictions.

Standard contract provisions could be developed by the professional associations in consultation with the CRPC and the FCMC. The CRPC and the courts have generally taken the view that standard contracts might be unfair because they typically cannot be discussed, clause by clause, by the financial institution with the consumer before being signed, and thus they might include unfair contract terms for consumers. For the consumer, the only choice is either to accept the terms of the contract without modification or not to obtain the financial service. Thus, one alternative would be to develop standard contract provisions that both protect the financial institution and are fair to the consumer. If the phrasing is developed by the professional associations and approved by the CRPC and FCMC, the standard contract provisions will meet the test needed to satisfy both financial institutions and consumers.

Standard contracts may also protect financial institutions from the risk of legislative changes. In response to a public outcry, the Consumer Rights Protection Law was amended in June 2009 to state that a financial institution can no longer revise certain consumer contract terms, except in cases of material breaches of the contract. Material breaches are defined as cases where: (1) debt service is overdue for more than 60 days or more than three times in a given year, each time for more than 30 days; or (2) no loan agreement had been signed. For mortgage borrowers who were not in material breach, the financial institution is no longer permitted to request additional collateral. The revision of basic consumer protection legislation in this way could likely have been preempted, however, had financial institutions consistently used standard agreements or standard contract clauses that already were reviewed by the CRPC and the FCMC.

Business Practices

Codes of conduct, or consumer protection codes, could also help to improve the practices of financial institutions vis-à-vis their retail customers. Consumer protection codes could be developed for each segment of the financial sector or one could be prepared for use across the financial sector. Codes should be as similar as possible across segments, ideally based on basic common rules for all segments and only specifics added for each individual segment, to make sure conditions are equal for financial products that have similar features but are legally different (such as mutual funds and unit-linked insurance). Codes of conduct have already been developed by the Association of Latvian Commercial Banks, the Insurance Association and the Association of Leasing Companies. However none of the codes is well-known, even to the members of each association. The value of a code of conduct is its widespread distribution so that consumers know that, in principle, financial institutions have agreed to provide minimum levels of service and to respond to complaints and disputes. The codes of conduct should be placed in bank branches and retail offices of financial institutions and on their websites. Consumers should be advised that if a

financial institution fails to comply with the code, a complaint can be submitted to the institution, the professional association and the CRPC. There should be a strong mechanism to investigate breaches of the codes of conduct, including the possibility that these breaches be publicized and that the financial supervisory agency use these breaches as warning signals for further issues to look at.

The application of a policy of “comply or explain” could be useful to strengthen the enforcement of codes of conduct. Under this policy the financial institution is assumed to comply with the code of conduct, otherwise the financial institution would have to explain reasons for non-compliance. Non-compliance and non-explanation would be considered a misleading business practice and be subject to sanctions as such. The same policy could be applied to standard contract provisions, where the need to deviate from a standard contract provision would have to be explained.

In Latvia, codes of conduct may be particularly effective. Although such codes are generally voluntary in nature, consumer associations can cite the codes when negotiating with financial institutions on behalf of consumers. Also the Unfair Commercial Practices Prohibition Law includes in the definition of unfair practices, cases where a financial institution does not conform to standards of professional diligence. Where a professional association has formally adopted a code of conduct for its members that code *de facto* sets a standard of professional diligence.

Personal liability of an officer of a financial institution officer for his or her improper dealings with a retail consumer should potentially be the subject of both civil and criminal proceedings. At present, only criminal proceedings are applicable. In accordance with the Latvian Criminal Code, a crime is committed by anyone who, in providing a paid service to a consumer, fails to comply with legal or regulatory requirements, thereby causing the consumer “substantial harm”. In the most egregious case, the individual service provider can be subject to imprisonment for as much as five years. When a breach of these duties occurs, proceedings for the payment of damages can be commenced in civil courts. With resort to Latvian civil court jurisdiction, personal liability should also be incurred by any staff member of a financial institution who, through a breach of his or her duty, causes harm to a consumer.

Consumers of retail financial services who submit inaccurate financial information or misuse loan proceeds should also potentially be the subject of parallel civil and criminal proceedings. By the Latvian Criminal Code, a consumer who provides false information to a creditor, or uses the proceeds of a loan for purposes other than those stated in his or her loan agreement, may be subject to imprisonment for up to five years. Under the Credit Institutions Law, a borrower has a duty to provide to his or her creditor complete and accurate information about his or her financial situation and property, including encumbrances on such property. It is not clear, however, what the remedy is for a breach of this duty. Also, in addition to those penalties applied by the State under criminal law, a general provision in the Civil Code should deal with remedies for a financial institution which suffers loss as a result of the same false information from a retail consumer.

It would be advisable to place a 14-day cooling-off period on the purchase of financial services. The EU Directive on Distance Marketing (incorporated into the Consumer Rights Protection Law) requires that contracts in respect of all financial services sold by telephone or over the internet have provisions for a 14-day cooling-off period to allow the consumer to change his or her mind and cancel the service without penalty. Similarly the EU Consumer Credit Directive, approved in 2008, includes a 14-day cooling-off period (transposition of the Directive into Latvian is under preparation). For insurance services, a 15-day cooling-off period is in place

for life contracts of six months or longer. However the law also requires that the termination of a contract be notified no later than 15 days before the date the contract is effective. This provision allows financial institutions to avoid the cooling-off period in practice for contracts where the time between the signing date and the effective date is less than 15 days. Cooling-off periods are an important mechanism for protecting consumers from high pressure sales tactics and should be established for all financial services which include a long-term savings component (and thus large commissions for sellers of the services). However one caveat is in order. Some financial services involve market risk, for example, on a mortgage where the lender locks in a fixed funding cost and must unwind the contract if the service is later cancelled. For contracts with such types of market risk, consumers who cancel their contracts during the cooling-off period should be required to compensate the financial institution for any out-of-pocket losses.

The FCMC should strengthen the requirements for administrative procedures regarding account handling and maintenance, as well as requirements of due diligence when offering a product or service to a consumer. Across the financial sector, but particularly in the insurance area, detailed regulations are needed in order to instruct financial institutions on the administrative procedures for such matters as the distribution of customer account statements at least annually. There should also be clear rules for financial institutions to gather, file and record sufficient information from consumers and ensure that the product, service or recommendation offered by the institution is appropriate to the consumer.

Emphasis should also be placed on strengthening the training and certification of those who work with the retail public. Officers who work in financial institutions generally are respected by the public and financial consumers tend to rely on the advice provided by officers of financial institutions. In Latvia, each financial institution is responsible for the training and certification of staff who work with retail customers and no other training or certification is required by the professional associations or the supervisory agencies. In their disputes, however, consumers typically complain that the responsible officers of financial institutions were unable adequately to explain the services being sold. In at least one case, the officer recommended to the customer that he not disclose his additional indebtedness, since the disclosure of additional financial obligations would have made the consumer ineligible for a bank loan. One way of eliminating such abusive practices would be to set a three-tiered level of training for officers of financial institutions. For those who sell only simple services, training by the financial institution would be sufficient. However, for those officers who sell complex financial services to retail clients, the officers should be required to attend training provided by the relevant professional association with a curriculum approved by the FCMC.

Financial institutions should be legally responsible for any statements made in their advertising and the content of the advertising should be monitored by the CRPC. Financial institutions should be responsible for offers they make in their advertising, whether by means of newspaper, radio, television or otherwise. Financial institutions should also bear responsibility for actions their agents make when advising or offering a product or service to consumers. Commercial advertising, including that of financial institutions, is supervised by the CRPC which is responsible for enforcing the Law on Advertising and the Unfair Commercial Practices Prohibition Law. While staff is limited, the CRPC should from time to time review advertisements made by financial institutions. In many countries, financial institutions place large font advertisements claiming zero percent borrowing rates and hide the APR in the small font fine print. In other cases, they may disclose key information in small print that moves quickly at the bottom of a television advertisement. The CRPC should monitor to ensure that such advertising does not occur.

The credit reporting system should be further strengthened. The setup of the Credit Register by the Bank of Latvia was an important step to improve the credit reporting system. The credit register—currently available only to banks—was established only in July 2008. Thus, the credit reporting system is still under development. As of March 2009, it officially covered less than four percent of the Latvian population, which is one of the lowest levels in Europe. Furthermore, the credit register is not yet accessible by non-bank credit institutions, although plans are underway to expand access to the non-bank credit sector. In the interim, non-bank financial institutions, such as debt collectors, have created their own private credit bureaus for their internal credit risk analysis. However, the data in the private credit bureaus is not consolidated with that of the credit register. Furthermore, improved regulation of private credit bureaus is needed, particularly in areas such as the minimum time for the retention of data. (The credit bureaus generally keep data for ten years but this is due to the 10-year statute of limitations rather than specific regulations on data retention.)

Improved regulation is also needed for debt collection agencies. Throughout central and eastern Europe, the rise of consumer finance has also resulted in an increase in the number of companies collecting bad debts on behalf of creditors. Debt collectors may play a valuable role, providing a way in which lenders can sell non-performing loans and thus increase liquidity in the financial system. However, similar to all financial institutions, debt collectors should be subject to a minimum level of business conduct supervision. In Latvia, debt collection agencies are not required to be licensed or even registered with a financial supervisory agency. Even leaders in the industry can only guess at the number of debt collection companies operating in Latvia (estimated at 75 to 100 firms). At a minimum, the leading debt collection agencies should establish an industry association that lists the companies that are association members. An association of debt collection agencies should also adopt a code of conduct in order to establish minimum acceptable rules of conduct for debt collection agencies. At present two debt collection agencies follow the Code of Ethics and Code of Operations of ACA International, the Association of Credit and Collection Professionals.

Consideration should be given to establish debt counseling centers. Latvia ranks ahead of many central European countries in approving legislation on personal bankruptcy. The new Insolvency Law of 2008¹⁸ included a section on personal bankruptcy, thus providing at least one option for consumers. However, prior to applying for bankruptcy protection, heavily indebted consumers should have access to counseling centers that can provide advice for consumers before they apply to the court. In the United States, the 2005 revisions to the Bankruptcy Code¹⁹ require that before applying for bankruptcy, consumers must attend counseling sessions on various legal alternatives available to them. Such mandated counseling often has little impact on the behavior of US consumers. However, in countries that lack a long tradition of consumer finance, such mandatory training has proven to be helpful for consumers in reviewing their financial options.

Dispute Resolution

Finding effective and fair ways of resolving disputes between financial institutions and their retail customers lies at the heart of effective consumer protection in financial services. For most retail customers of financial institutions, the amounts involved in a dispute are relatively

¹⁸ The new Insolvency Law, effective as of 1 January 2008, replaced the Law on the Insolvency of Undertakings and Companies (adopted on 12 September 1996).

¹⁹ The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Public Law No. 109-8, was enacted on April 20, 2005 and revised Title 11 Bankruptcy Code of the United States Code.

small (generally under Euros 500 equivalent). However, failure to resolve disputes quickly, efficiently, transparently and professionally undermines public confidence in financial institutions—and reduces the trust that is needed by financial institutions if the sector is to be stable and resilient.

All Latvian financial institutions with retail customers should be obliged to maintain—and to publicize the existence of—a consumer complaints department. The Latvian legislation already provides for some important legal protections for consumers. The Cabinet of Ministers Regulation on the Procedure for Submission of Complaints²⁰ requires that sellers of goods and service providers submit written responses to consumers within 10 days of the time a complaint is submitted. However, this requirement does not apply to financial institutions. New amendments to the Consumer Rights Protection Law would require banks to respond within 30 days to consumer complaints related to debt restructuring and other specific matters. This is a useful first step. Most banks and other major financial institutions have a designated office, such as a public relations department, that is responsible for receiving complaints from retail customers. However, the contact information for the department is typically not well-publicized. All financial institutions with retail customers should be required to designate a department (or at least an officer) who is officially responsible for receiving and addressing consumer complaints—and the contact information with telephone number, fax number and email address should be provided in writing to consumers when they open any account for a financial service. In addition, as part of its work on prudential supervision, the FCMC should request from all financial institutions quarterly statistics on the number of consumer complaints received and processed, the nature of complaints, the average time spent to resolve the disputes presented by consumers and the type of resolution offered to the complainant.

Statistics on complaints submitted to government agencies should be analyzed and published. Complaints represent an "early warning signal" for potential issues throughout the financial sector. The Consumer Rights Protection Law allows for complaints to be submitted to any of several agencies, although the CRPC receives the bulk of the complaints. Complaints on retail securities (including transactions made by private pensions and investment funds) are generally presented directly to the FCMC. When these complaints are presented to the CRPC, they are transferred to the FCMC. However, statistics are not consolidated. Nor are they analyzed in a systematic way by the FCMC or the CRPC in order to determine the common sources of complaints.

Although the number of complaints has been rising, it is still relatively low. The number of consumer complaints regarding financial services in Latvia has more than doubled from 2007 to 2009. In particular the number of complaints received by CRPC regarding consumer credit increased from 30 in 2007 to 256 in the first nine months of 2009 (see Table 9).

²⁰ Cabinet of Ministers Regulation No. 631 on the Procedures for the Submission and Examination of Consumer Claims Regarding the Non-conformity of Goods and Services with Contract Provisions ((1 August 2006).

Table 9: Consumer Complaints regarding Financial Services in Latvia

	2007	2008	Sep-2009
Received by CRPC			
Consumer Credit	30	106	256
Insurance	15	33	13
Other Financial Services	9	18	12
Total Received by CRPC	54	157	281
Received by FCMC			
Credit institutions	101	109	172
Insurance	89	110	86
Securities	15	14	7
Pension Funds	2	3	0
Other	12	13	19
Total Received by CRPC	219	249	284
Total Complaints	273	425	565

Sources: CRPC, FCMC

The low number of complaints regarding financial services, however, suggests that consumers do not have sufficient confidence in dispute resolution mechanisms in Latvia. In countries where institutions have been established to address complaints regarding retail financial services, the number of complaints generally increases significantly as has been seen in the years after the establishment of the United Kingdom's Financial Ombudsman Service. As seen in Table 10, the number of financial disputes for even other small countries such as Malta, are about 250 per year. Although the number has been rising, the relatively low number of complaints regarding financial services in Latvia suggests not that consumers are highly satisfied, but rather that if they take the time to complain, they have little confidence that their complaints will be resolved to their satisfaction. In other cases, consumers may not be aware of the options available for dispute resolutions. The February 2006 survey by GE Money found that some 66 percent of financial consumers were not then familiar with the available dispute resolution mechanisms.

Table 10: Consumer Complaints Received by European Complaint Services in 2007

Complaint Service	Number of Complaints
UK Financial Ombudsman Service	116,600
Italian Banking Ombudsman	4,000
French Insurance Mediator	4,000
Belgian Insurance Ombudsman	3,400
Hellenic Ombudsman for Banking–Investment Services	1,500
Consumer Complaints Scheme of the German Association of Private Building Societies	650
Finnish Securities Complaint Board	250
Consumer Complaints Manager of the Malta Financial Services Authority	250

Source: European Commission, *Alternative Dispute Resolution in the Area of Financial Services*, Consultation Document, MARKT/H3/JS D(2008).

The CRPC should take measures to help consumers become aware of their legal rights in case of complaints with financial institutions. Consumers should be clearly informed of their

rights to complaint to a financial institution or to the CRPC in case they are not satisfied with the response offered by the institution. In 2009 the CRPC established a toll-free hotline, where consumers from anywhere in Latvia can call to obtain information about all consumer protection matters. Consideration could be given to set up a specific option for financial services in the future. Another approach would be to create brochures that describe legal rights of financial consumers in simple and plain language—and provide information on how to contact the CRPC. The rules for complaints handling should be similar across financial segments to make it easier for consumers to complain. The CRPC should also actively present important complaints and their resolution in the media to educate the public and show that it is possible to achieve a solution when a consumer actively fights for his or her rights. Media coverage of consumer mistreatment could also play an effective role in disseminating and developing good practices, by “naming and shaming” financial institutions that mistreat consumers. However, journalists ought to be educated to understand not only financial products and services but also the legal framework for financial consumer protection, so that they are able to cover the stories properly.

However, a key issue is to separate different types of complaints. Complaints may take any of several forms. In most countries, the bulk of complaints are in fact inquiries, where for example, consumers may want to know why their bank has refused to extend them credit. Or they want to know about their legal rights in case they have become unemployed and would like a few months grace until a new job is found. Or they seek advice on shopping for third-party motor liability insurance. Other complaints are based on issues of fairness: consumers believe that their financial institution is behaving inappropriately, say, by charging too much for a credit. Yet still other complaints amount to clear legal disputes, where the consumer has a different interpretation of the contract than does the financial institution.

Consumers need a central body, such as the CRPC (or an independent financial ombudsman), where they can submit their inquiries, complaints and disputes and can promptly receive an answer, advice or just additional information. As an initial step, the CRPC should maintain a log of all telephone calls, as well as telephone and fax complaints and analyze the nature of these complaints. Based on this analysis, the CRPC should set up programs that address the common features—by providing additional consumer education, working with local government administrations to provide advice to consumers in local centers, or making consistent decisions in respect of similar, specific disputes.

Over time, consideration should be given to establishing an independent ombudsman for retail financial services. Both the Association of Latvian Commercial Banks and the Insurance Association have established ombudsmen for their sectors. However, the Banking Ombudsman only makes recommendations in respect of disputes regarding payments and other electronic transfers of cash and the Insurance Ombudsman only makes recommendations in cases related to property and motor insurance, provided in both instances that the parties to the dispute have agreed to seek out such recommendations. These ombudsmen are, however, set up and funded by the respective financial professional association and therefore may be considered to favor financial institutions at the expense of retail customers. This might be one of the reasons why the Ombudsmen generally receive only some 20 to 40 cases a year combined. As a result, they have little impact on the public perception of the financial sector. A still greater issue is that neither other banking and insurance products nor other parts of the financial services industry—from debt collectors to pawn-shops to payday lenders to leasing companies—are covered by any financial sector ombudsman. The question of establishing an independent statutory financial services ombudsman needs careful consideration, with a complete review of the costs and benefits and a clear system established for the sustainable funding of such office.

Latvia should also join FIN-NET. FIN-NET is a network of financial dispute mechanisms and national out-of-court complaint schemes for European countries. Latvia should be part of this Europe-wide network once financial out-of-court complaint and dispute resolution mechanisms are adequately set up to apply for membership. It is worth to note that CRPC has participated in FIN-NET meetings in 2009, and it should continue doing so.

Financial Education & Financial Capability

The Consumer Protection Policy of the Latvian Government includes programs of consumer education, including financial education. The Consumer Protection Program for 2005-2007 included as one focus area the provision of information on consumer protection and the promotion of consumer education. One of the activities was a project known as “Prudent Borrowing”, a competition for secondary school students regarding responsible consumer credit (how to spend 100 LVLs wisely), organized in 2007. The activity was funded by the CRPC and organized by the umbrella consumer association PIAA, with the support of Money Planning Center, NGO founded in 2007 by GE Money and the Riga International School of Economics and Business Administration. The contestants were evaluated by a committee of experts from non-governmental organizations, the Ministry of Economics, the Association of Latvian Commercial Banks, the Money Planning Center, and GE Money.

As part of consumer education and awareness, the CRPC should also prepare booklets and leaflets that provide common-sense advice and assistance for financial consumers. For example, the CRPC might prepare a leaflet on steps that consumers should take when they first experience financial difficulties, such as loss of employment or hardship in re-paying a housing loan. It may be helpful to review the approaches taken by the United Kingdom’s Financial Services Authority through its consumer finance website (www.MoneyMadeClear.fsa.gov.uk) and adapt them for Latvian consumers.

The financial supervisory agencies could increase their work in improving consumer awareness of the risks and rewards of financial services. In order to raise public awareness on issues related to central bank activities, in early 2005 the Bank of Latvia created “Money World” as a financial education and information center. Its target audience is students older than 14 years. On average, 600 students visit Money World every month. The Banking Academy (BA) School of Business and Finance (a government-funded institution of higher education which also trains banking professionals) also engages in consumer awareness activities, by conducting conferences and seminars. In 2007, BA School of Business and Finance sponsored a project developed by students, which resulted in a booklet describing key information on mortgage credit for the average consumer (*Kas ir kredīts*). By contrast, the FCMC does not publish information to improve consumer awareness of financial services—but they should. Such information should cover general descriptions of the costs, risks and benefits of using financial services.

Consumer associations should help to develop financial consumer awareness not only in Riga but throughout the country. Consumer associations are generally the first instance where consumers go for advice and information, especially in remote areas of the country. Consumer associations should be allies of the CRPC in protecting consumer rights and providing information for consumers.

Some private sector organizations provide financial education but more could be done. Money Planning Centre, an organization created by GE Money in 2007 with the objective of

educating consumers on financial planning and other financial matters, has recently published a book that explains basic financial issues in simple terms. Money Planning Centre has also signed a Memorandum of Agreement with the agency that oversees libraries in Latvia, in order to distribute this book at no cost to all libraries. This project was financed by GE Money and the insurance company If Latvia. Money Planning Centre has conducted other activities focused on educating children regarding financial issues, such as a competition for children in 1st to 4th grades based on paintings of what children understand about money. Also, in November 2009 Swedbank set up the Institute of Private Finances in Latvia. The Institute was originally established in Sweden more than 50 years ago, and in 2009 three other country offices were set up (in Lithuania in January 2009, and in Latvia and Estonia in November 2009). The Institute operates as an independent part of Swedbank and its main objective is to help raise people's awareness of management of their personal finances. One of the first activities of the Institute in Latvia has been the conduction of surveys at schools, to obtain information about the level of basic financial knowledge in school students.

Improvements could be made in the frequency and detail of information given from regulators to the media regarding financial services. Two main newspapers specialize in financial news (one in Latvian and one in Russian). In addition, some financial articles have recently been included in weekly general magazines such as *Ieva*. Two TV stations (LTV and TV3) broadcast daily shows based on real complaints that Latvian people share with the TV stations about different types of products and services. Recent months have seen an increase in the number of complaints regarding financial services discussed on these shows, particularly by individuals who co-signed loans on behalf of family members or friends and who did not realize the full implications of doing so until the lender asked for payment directly from the co-signer. These shows usually invite an officer of the CRPC and/or the FCMC to provide comments on the cases. In addition, the Bank of Latvia sponsors a TV show dealing with news on economic and financial issues. On the radio, Latvian Radio Station's show "*Ka labāk dzīvot?*" or "How to live a better life?" also touches upon financial issues and calls experts from institutions like the CRPC or Money Planning Centre to ask for their opinions. The programs are very useful in providing consumer education—and increasing consumer awareness—but more could be done. Good media coverage of consumer protection issues is an effective tool to provide consumer education, but journalists ought to be educated and trained to make sure they are equipped to cover consumer protection issues properly and effectively.

The Ministry of Education should consider the inclusion of financial education topics in the public school curriculum. Learning about the importance of financial health needs to start at an early age—before the age of 12, when children begin to adopt life-long values. The public school curriculum in Latvia does not include the topic of financial education at any level. The elementary school subjects "Introduction to Economics", "Social Science and Home Economics and Technology" and the secondary school subjects "Fundamentals of Business Economics" and "Politics and Law" indirectly include some information on consumer protection and financial and economic issues, but there is no focus on financial education or financial consumer protection as such. There are no materials related to these issues and teachers are not trained to teach these issues.

Financial education should also be provided to adults. Some adult-education regarding the use of financial services is provided through the online DOLCETA (Development of Online Consumer Education Tools for Adults) program which has been translated into Latvian. Consumer training regarding financial services could also be provided, however, through professional associations and financial institutions, and it should help consumers understand the terms and conditions of the financial contracts they sign. Training for adults should be conducted

on "teachable moments" such as the time when a consumer becomes a first-time homeowner and signs a mortgage. Planning for retirement is another useful teachable moment. It may also be helpful to conduct "mystery shopping" to see the issues that arise for consumers as they try to buy financial products and learn about the risks and rewards of different products.

A nationwide financial literacy survey would provide a useful baseline assessment of the current levels of financial capability. Several countries, including the United Kingdom, Ireland, Australia, Canada and Russia, have conducted nation-wide surveys of households assessing their levels of financial literacy, as well as their values and behaviors (taken together called "financial capability"). The survey should be segmented by age, gender, levels of formal education, and geographic area, as well as by rural versus urban areas. Segmentation will provide policy-makers with insight into the key issues for financial consumers as they consider their capacity to meet their obligations and plan for their financial futures. Such a survey should then be repeated in three to five years, to see if consumer protection and financial education programs have had the impact that was anticipated—and if the programs should be further modified.

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Annex 1: Key EU Directives on Financial Consumer Protection and Applicable Latvian Laws

CELEX Reference	EU Directive	Supervisory Agency	Latvian Law
3 1987 L 0102	Directive on Consumer Credit, 1987/102/CEE, as amended	CRPC	Consumer Rights Protection Law
3 2008 L 0048	Directive on Consumer Credit, 2008/48/EC, repealing Directive 87/102/EEC	n.a.	Under preparation
3 1993 L 0013	Directive on Unfair Terms in Consumer Contracts, 1993/13/EEC	CRPC	Consumer Rights Protection Law
3 2005 L 0029	Directive concerning Unfair Business-to-Consumer Commercial Practices in the Internal Market, 2005/29/EC	CRPC, Health Inspectorate, Food and Veterinary Service	Unfair Commercial Practices Prohibition Law
3 1998 L 0027	Directive on Injunctions for the Protection of Consumer Interests, 1998/27/EC	CRPC	Consumer Rights Protection Law, Civil Law
3 1985 L 0577	Directive on Doorstep Selling, 1985/577/EEC	CRPC	Consumer Rights Protection Law
3 2000 L 0046	E-Money Directive, 2000/46/EC	CRPC	Consumer Rights Protection Law
3 1997 L 0007	Directive on Protection of Consumers in Respect of Distance Contracts, 1997/7/EEC	CRPC, Competition Council, National Radio and TV Council, Health Inspectorate	Consumer Rights Protection Law
3 2002 L 0065	Directive on the Distance Marketing of Financial Services, 2002/65/EC	CRPC	Consumer Rights Protection Law
3 2006 L 0114	Directive on Misleading and Comparative Advertising, 2006/114/EEC	CRPC	Advertising Law
3 1994 L 0019	Directive on Deposit Guarantee Schemes, 1994/19/ EC	FCMC	Deposit Guarantee Law
3 1997 L 0009	Directive on Investor Compensation Schemes, 1997/9/EC	FCMC	Investor Protection Law
3 1985 L 0611	Directive on UCITS, 1985/611/EEC, as amended	FCMC	Law on the Financial Instruments Market
3 2004 L 0109	Directive on Transparency, 2004/109/EC	FCMC	Credit Institutions Law
3 2004 L 0072	Directive on Market Abuse, 2004/72/EC	FCMC	Law on the Financial Instruments Market
3 2004 L 0039	Directive on Markets in Financial Instruments, 2004/39/EC (MiFID)	FCMC	Law on the Financial Instruments Market
3 2002 L 0083	Directive on Life Insurance, 2002/83/EC	FCMC	Insurance Contract Law
3 1992 L 0049	Directive on Non-Life Insurance, 1992/49/EEC		
3 2002 L 0092	Directive on Insurance Mediation 2002/92/EC	FCMC	Insurance Contract Law
3 2002 L 0058	Directive Concerning Processing Personal Data and Protection of Privacy in the Electronic Communication Sector, 2002/58/EC	DSI	Personal Data Protection Law
3 1995 L 0046	Directive on the Protection of Individuals with regard to the Processing of Personal Data, 1995/46/EC	DSI	Personal Data Protection Law