

## **Simplifying financial information**

### ***The legal framework***

Candice Burt, June 2007

### ***Background to plain language legislation in South Africa***

#### **Principles for transforming justice**

To understand the intention behind South Africa's consumer-focused legislation, we must explore what it aims to remedy. In his opening address at a 1995 seminar called *Plain language, the law and the right to information*, the then Minister for Justice, Mr Dullah Omar, spoke about the transformation of justice. He outlined several key principles as being important to achieve that transformation: the principle of access to justice; the principle of participation; and the principle of empowerment. He called for 'plain, simple and understandable language' in the country's laws, in court judgments, in consumer documents, in radio and television broadcasts. He referred to plain language as "democratising language".

Since then, the policy- and lawmakers in South Africa have had their hands full with writing laws that will ensure the transformation Justice Omar spoke of.

#### **Plain language in the Constitution and Bill of Rights**

In 1996, the drafters of the Constitution of South Africa took a decision to write the Constitution and its Bill of Rights in plain language. The reason was simple enough: the Constitution should bring about the equality it talked about – between people of different races, different classes, and different education levels. In other words, the Constitution must be understood by the ordinary citizen.

#### **Drive for consumer protection in laws**

South Africa has recently entered a new era of protectionist legislation aimed at balancing the negotiating power between those who provide products and services and the ordinary citizens who receive them. These principles are embedded in both the National Credit Act, which became fully operational at the beginning of this month; and the Consumer Protection Bill which we understand will come into effect in early 2009. The purpose of these laws is to ensure consumers can make informed choices about the products and services they want and need, without being seduced by misleading and deceptive business practices.

#### **Simplification of financial information and consumer education**

Nowhere is information more complex than in the multitude of financial products and services available in South Africa. The financial services industry itself is not consistent with product offerings and there is a bewildering range of terminology.

There are several laws governing the simplification of financial and other information and the education of consumers. This morning, I will be discussing those laws as well as international and local trends in simplification of financial information.

## ***International trends –consumers making informed decisions***

Despite its recent appearance in South Africa's statute books, the notion of 'plain language' is not new. Sometime in the 5<sup>th</sup> century BC, Confucius declared 'clearness in language is everything'. For centuries there have been proponents of plain language, rallying against officialese, legalese and bureaucratese. In those same centuries, there have been those who have obfuscated, complicated and deceived. Trends in language usage change with the political and social discourses of the day.

And so we start – not in the 5<sup>th</sup> century BC – in the 1970s in the USA and the UK. The history I am giving to you is a sweeping one: my aim is to give you a background to the current drive for consumer education and simplified information in all spheres but especially in financial services. By looking at the international trends we can understand where plain language comes from and which direction it may go in the future.

On both sides of the Atlantic, people's power was driving the cause for plain language:

### **The UK: consumer activism – the fight for clear communication**

#### ***Plain English Campaign***

In the UK, the plain language movement was launched in a hail of confetti – confetti made up of the shredded government welfare forms and regulations. Chrissie Maher, founder of the Plain English Campaign, set up a shredding machine in Parliament Square and dropped into it every form and regulation that she considered was unclear for the ordinary citizen.

Challenging the concept that 'ignorance of the law is no excuse', Maher claimed that the people could not help but be ignorant of the law because the language of the law was impenetrable.

#### ***Government rewrite project***

Government took notice of the drive for people's power - and over the next decade it rewrote 58 000 forms in a comprehensive plain language project. Its main aim: to empower its citizens.

#### ***The Financial Services Authority***

The Financial Services Authority (FSA) in the UK has been the most active organisation as far as financial information is concerned. As the watchdogs of the financial services industry, they have the power to challenge unfair contract terms. According to the FSA, a standard term in a contract with consumers 'must be expressed in plain and intelligible language. A term is open to challenge if it could put the consumer at a disadvantage because he or she is not clear about its meaning - even if its meaning could be worked out by a lawyer. If there is doubt as to what a term means, the meaning most favourable to the consumer will apply.'

The FSA also initiated the Raising Standards Quality Mark Scheme. Through this project, a mark is awarded to financial services companies that meet certain promises to consumers. The broad promises are:

- Clarity and comparability of information
- Appropriateness of the products purchased
- Customer service.

Each promise has a thorough set of assessment criteria against which the company is measured. For consumer documents, upfront summaries, plain language, clear style and design are just a few of the criteria for the first promise.

The FSA has now moved beyond merely requiring financial services companies to write in plain language. The Treat Customers Fairly initiative, begun in 2004, sets out certain high-level principles that ensure regulated companies treat their customers fairly.

Again, the campaign stresses the importance of giving consumers correct and clear information in plain language upfront and at the time of the sale to help them to make informed choices.

The deadline date for implementation of the initiative for regulated companies was May this year. The FSA reports that many financial services companies in the UK have met that deadline.

## **The USA: Recognising commercial value**

### ***Citibank – a business imperative***

The plain language movement in the UK started with campaigns urging government and companies to 'do the right thing'. 'Doing the right thing' is now a much broader and regulated issue. In the USA, the plain language movement gained ground first as a business imperative in the financial services industry and later similarly became regulated (albeit more stringently).

Possibly the most famous – and certainly most-quoted – early plain language commercial document is the Citibank of New York consumer loan note. It was produced in 1975 in response to the high volume of litigation the bank engaged in over the document's predecessor, a less-than-plain 'promissory note'. A promissory note is a document signed by a borrower promising to repay a loan on agreed terms. Because of the impermeable language, the promissory note was open to a multitude of interpretations and gave no certainty to the bank that it could recover its debts from customers.

The bank claimed two major benefits of the new consumer loan note:

- it reduced substantially the amount of litigation the bank brought against customers to recover the debt;
- it helped to increase the bank's market share in the 1970s and 1980s.

Of most interest to those concerned about precision of plain language, the bank claimed that no cases it brought against customers to recover debts on the new consumer loan note involved a dispute over wording.

The First National Bank of Boston and the National Bank of Washington followed suit the following year with plain language loan documents.

### ***Plain language promoted as a civil right***

In 1978, the US federal government encouraged regulation writers to be less bureaucratic. President Carter called for government regulations that were 'easy-to-understand by those who are required to comply with them.'

Efforts to write plain regulations were initially sporadic but over the next two decades they were introduced in some 35 states in the US.

In the late 1990s, President Clinton stepped up the drive for plain language, requiring all regulations passed after 1 January 1999 to be written clearly. Vice President Al Gore was charged with overseeing the initiative. Believing that 'Plain Language is a civil right', he awarded monthly 'No Gobbledygook awards' to federal employees who turned 'officialese' into plain language that citizens understand.

### ***The Securities and Exchange Commission***

The Securities and Exchange Commission, charged with protecting investors and maintaining the integrity of the securities markets, requires that information in prospectuses be clear, concise, and understandable. The *SEC Plain English Handbook* published in 1998, is still one of the most useful guides on how to write in plain language. Warren Buffet, financial guru, wrote in the preface of the *Handbook*:

"[When I write], I picture my sisters, highly intelligent, but not experts in accounting or finance. They will understand plain English, but jargon may puzzle them. My goal is to give the information I would wish to receive if our positions were reversed.

In the wake of the Enron and other scandals, the SEC has declared war on complexity in disclosure. It aims to eradicate boilerplate clauses in legalese; to introduce easy-to-navigate web pages; and to reduce the complexity of the accounting rules and regulations.

### ***Financial literacy programmes***

From around 2000, there has been a trend towards educating consumers about over indebtedness and the US's spiralling debt problems. Financial literacy programmes have been introduced in the school and colleges in an attempt to encourage and empower consumers to be responsible.

## **South Africa's legislative agenda: transformation**

While the international trends have been about openness and transparency, what has happened in South Africa since Justice Dullah Omar made his statement about transforming justice.

Several acts were passed.... the Long-term Insurance Act and Short-term Insurance Act, (both passed in 1998) set out to control the activities of insurers and intermediaries. Shortly afterwards the Financial Advisory and Intermediary Services Act introduced tighter governance for financial services providers. There are plain language provisions in each of these three Acts which require that information provided to a customer be “in plain language, avoid uncertainty or confusion and not be misleading” and “be in a clear and readable print size, spacing and format.”

## **Institutional framework promotes plain language**

### **The Financial Services Board and Life Offices Association**

Self-regulation also plays a part. The Financial Services Board is currently revisiting its consumer education policy and the Life Offices' Association has a complementary education policy to help consumers make informed decisions about long-term insurance products. There are speakers later on today who will discuss the Financial Sector Charter's objectives to educate consumers.

### **Code of Banking Practice**

In 2000, all the major banks in South Africa adopted the Code of Banking Practice which set out fundamental principles of their relationship with customers. Among other undertakings, the banks promised to:

- make information available to customers about services and products in plain language and give help on any aspect which customers do not understand;
- ensure that all written terms and conditions are fair and clearly set out the customer's rights and responsibilities in plain language
- help customers to understand the basic financial implications of the bank's products and services;
- help customers to understand how their bank account works.

The banks were fairly ambitious by giving themselves until October 2000 to achieve this goal, a fact that the then Banking Adjudicator, Adv Neville Melville, highlighted in the Office of the Banking Adjudicator's Annual Report in 2000:

“Banks have wasted an opportunity to prove their good faith by failing to meet their deadline of October 2000 to ensure all their documents are written in plain language. The continued use of terse legal terms and bank-specific jargon disadvantages a substantial category of lower and middle-income earners who contribute to much of the banks' profits.”

It is not clear whether the banks have set themselves new date to honour their promises, but the National Credit Act and later the Consumer Protection Bill may do that for them.

## **The National Credit Act**

One of the purposes of the NCA is to correct imbalances in negotiating power between consumers and credit providers:

- educating consumers about credit and consumer rights
- giving adequate disclosure of standardised information so they can make informed choices
- protecting consumers from deception and from unfair conduct. [section]

So how does the NCA intend to achieve this purpose? It places several onerous obligations on credit providers to change their current business models and to amend their credit agreements. It imposes new debt enforcement mechanisms and affords consumers a rigorous dispute resolution process. Businesses must ensure their credit assessment procedures will stand up to the scrutiny of the National Credit Regulator as failure to comply can mean contracts, or parts of them, are declared invalid. This could have harsh implications for smaller businesses that may not be able to collect on debts. A possible future trend is the consolidation of the industry as smaller organisations may not have sufficient risk management programmes in place to compete.

### **Consumers' rights to receive information in plain language**

One of the new consumer rights set out in the NCA is the right to receive information in plain and understandable language. Although the other laws mentioned earlier have also contained plain language provisions, the National Credit Act is the first law to give a definition of plain language. In section 64, the NCA provides:

"A document is in plain language if it is reasonable to conclude that an ordinary consumer of the class of persons for whom the document is intended, with average literacy skills and minimal credit experience, could be expected to understand the content, significance and import of the document without undue effort, having regard to:

- the context, comprehensiveness and consistency of the document
- the organisation, form and style of the document
- the vocabulary, usage and sentence structure of the text
- the use of any illustrations, examples, headings, or other aids to reading and understanding."

### **Beyond words**

In the workshop on Friday, we will go through each element of this definition so I don't want to waste time here. However, it is important that this definition recognises that plain language is not just about the words. Vocabulary and usage are only two areas the credit providers must consider when writing their documents. And from the definition, these areas

are relatively low in priority. For a document to be in plain language the novice borrower must be able to understand the content and purpose of the document – in other words, why is the document important to the borrower; why must the borrower sign it; what are the consequences for that borrower?

From the definition, the first time debtor is assumed to have average literacy skills – in other words, we are dealing neither with an illiterate person nor a learned one. Of course, the issue of literacy skills in South Africa is a thorny one. The requirement to ensure that the consumers appreciate and understand the risks and obligations of entering into credit arrangements is set out in a later provision.

### ***Reader-testing and objective criteria***

To comply with the Act's definition of plain language and the "ordinary consumer" test, businesses may have to do reader-testing.

The National Credit Regulator may publish guidelines for methods of assessing whether a document is in plain language. We believe any guidelines will include various objective criteria based on international best practice (such as plain words, short sentences, and the active voice) as well as reader-testing. Any guidelines that do not include reader-testing would undermine the intentions of the Act and section 64.

### ***Comprehensive information and upfront summaries***

The definition also highlights comprehensiveness – have you given the borrower all the information they need to make an informed decision: for example, the amount of principal debt, any initiation fees, the interest, and taxes?

The Act later provides that quotes or pre-agreements must be issued to borrowers before they sign any credit agreement. The quote must show, among other things, the total costs of the credit at the front of the document in a prominent place. This is in line with the Raising Standards Mark Scheme from the UK where upfront summaries, for example, are required.

### ***Plain language: a declared right***

The right to receive information in plain and understandable language cannot be contracted out of by a consumer. This means that a business cannot merely insert a clause to the effect that the consumer declares that they understand and appreciate the purpose of the contract. Section 81 of the NCA requires credit providers to assess whether the borrower does in fact understand and appreciate the risks and costs of the proposed credit, as well as their rights and obligations under the contract. Businesses must develop evaluative mechanisms which are fair and objective to assess this understanding.

The Consumer Protection Bill contains a similar obligation. However, it requires that an ordinary consumer with "minimal experience as a consumer of the relevant goods and services" be able to understand and appreciate the documents.

## ***Business benefits to plain language***

The problem with a plain language programme that is driven only by compliance is that it runs the risk of implementing superficial, objective criteria that do not necessarily give information that truly helps the consumer to make informed decisions.

Rather, if business embraces the spirit of the transformative agenda of the legislature, and implements the plain language provisions with a sincere desire to empower, educate and enlighten consumers, it will find as a profitable and coincidental side-effect that there are many business benefits to doing so.

Other ways of driving plain language programmes will be dealt with later today when Frances Gordon discusses setting objectives for a plain language initiative.

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