Are Highly Satisfied Customers Fairly Treated Customers?

Yes _____ No ______ Maybe ✓

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Synopsis

The article describes why highly satisfied customers of financial services are not necessarily fairly treated customers. Customer satisfaction and mystery shopper satisfaction scores can be misleading and inadequate for measuring adherence to fair lending and consumer protection laws. Therefore, developing and implementing self testing programs that measure whether customers are treated fairly and equitably is imperative for a financial institution seeking to manage risk while building revenues and customer loyalty in today's marketplace.

Article

Government regulators, enforcement agencies and consumer advocates are taking a more aggressive and open ended approach to ensuring consumers do not face discrimination and unfair, deceptive acts and abusive practices when purchasing financial products. Many financial institutions are ill prepared. No longer can a financial institution rely just on following documented rules and regulations. A culture of fair and equitable treatment of the customer must exist.

Most financial intuitions and companies strive for excellent customer service and products. And why not, excellent customer service and superior products foster revenues and customer loyalty. Success in providing excellent service and products is assumed when high customer satisfaction marks or high net promoter scores are achieved. In fact many companies advertise high satisfaction scores as a means to attract customers by fostering trust and an image of meeting customer needs.

The assumption behind the use of customer satisfaction and net promoter measurement is that customers would not provide high marks if they were not treated fairly or received the best product. The assumption is based on a "buyers beware" culture and philosophy. The buyer judges whether or not the quality of service and product meets his or her needs or expectations. Consumers will reject companies providing faulty service and products. It is up to the consumer to make the best decision. If the consumer judges that his or her needs and expectations are met he or she is highly satisfied and will purchase the product and/or recommend. If the consumer is highly satisfied and will recommend the financial institution then the customer is treated well. The premise is false and can lead to significant risk for a financial institution or any company. Business risk in terms of lost revenues associated with providing unsuitable or faulty products. Reputation risk associated with customer complaints and charges of unfair or misleading acts or practices. Legal risk associated with violations of the law.

Let's take the example of Providian Financial. Providian marketed credit cards to consumers, including those with blemished credit ("sub prime"). The company's sales and market share grew dramatically in late 1990's. Consumers opened accounts and transferred their card balances to the company. Providian marketed its products through risk based scoring models and aggressively sold ancillary products. Providian and other companies trumpeted products like credit protection as a great way to avoid making payments when hospitalized or when out of work. This leveraged an important concern of low and moderate income consumers, financial security. The customer felt great about the product. She/he was highly satisfied. However, there were allegations the customer was not treated fairly. In many cases the allegations included the customer was not aware nor was it disclosed that there were a number of limitations that prevented the customer from benefiting from the product. For example, coverage was limited to the number of months premiums are paid and coverage was not available with regard to involuntary unemployment if the customer was self employed or paid less than three months of premiums or that coverage could be denied if the consumer paid more than the minimum to another credit card account.

Still another example is companies that leverage high customer satisfaction scores in advertising to help sell products. In the early and mid 2000's customer satisfaction measurement companies ranked mortgage lenders based on new borrower customer satisfaction. The highly ranked lenders touted their ranking and high customer satisfaction score. The rankings were based on surveys that queried new borrowers about their satisfaction with the loan process, including the application, representative, closing and problem resolution. The survey did not report on the needs discovery process, suitability of products offered nor the extent to which the borrower understood the product or whether the lender explained the features of some of the more problematic mortgages sold to consumers, for example Option ARM's, Stated Income Loans and Interest Only Loans. Many of the customers that purchased these products now allege they were sold loans they could not afford. In addition, the same customers allege they were not informed about various product features and the extent to which their monthly payment could vary depending on a change in the interest rate or the end of the interest only period.

New Challenges

So what should a financial institution do to ensure that its customers are treated fairly and highly satisfied?

The bank needs to integrate profit and revenue programs into a culture that treats customers fairly and equitably. Senior level management needs to actively promote the culture. This entails including fair and equitable customer treatment in its mission statement. Importance needs to be placed on providing customers with appropriate products and services that meet and exceed customer needs.

In order to adopt and then continually reinforce a fair and equitable customer treatment culture steps need to be taken to integrate it into the company's business plan and revenue goals. All employees, senior management, middle managers, back office employees and employees interfacing with consumers need to adopt the culture. Senior management needs to emphasize it and then incent employees based on it. Incentive plans and goals must be aligned with a culture designed to offer superior and appropriate products to consumers. Training programs must include a definition of fair and equitable treatment and why it is important to the company. Examples of unfair treatment and violations of consumer protection laws need to be communicated to business managers and branch employees. Sales and service standards and protocols that ensure fair and equitable treatment of customers need to be put in place. Adherence to these standards and adherence to consumer protection laws need to be monitored. Incentive and recognition programs should motivate adherence to standards fostering superior, fair and equitable treatment. All employees must recognize the risk to the company's success associated with treating customers unfairly and violating consumer protection laws.

These steps are particularly important given the changing regulatory environment, increased fair lending enforcement activities and the evolving emphasis on the part regulators on UDAAP and the subjective nature of determining whether an act is unfair, deceptive or abusive. Magnifying the effect of these changes is the emerging and growing importance of minorities. Financial institutions today need to be proactive in managing risk and developing products that meet and exceed customer needs.

Monitoring for New Age Compliance: Being Proactive and Testing for Fair and Equitable Treatment

So how does a financial institution determine whether or not its customers are treated fairly and equitably?

Let's look at some examples of how proactive monitoring can help a financial institution ensure fair and equitable treatment and avoid allegations of violations of the law and unfair, deceptive and abusive acts or practices.

Unsecured Lines of Credit and Cross Selling

Many institutions offer credit lines to cover checking over drafts and incent representatives to offer a credit line to cover overdrafts to the new checking account customer. The consumer over draws the checking account and monies are transferred into the checking account from the credit line to pay the overdraft plus any fees involved. In addition, the financial institution transfers more than the required amount to cover the overdraft through rounding. The consumer pays the interest on the funds advanced plus any fees. Is the consumer aware of the interest rate charged on the credit line, the fees incurred, the policy of rounding up and did the consumer agree to open the credit line? The customer who opened the checking account leaves the branch highly satisfied. Later in the relationship the customer complains. He or she was not aware of the interest charged on the credit line, the fees involved and the policy of transferring more than the amount of the over draft into the checking account. The bank may face allegations of misleading practices associated with the consumer not understanding the terms and conditions associated with the use of the credit line to cover over drafts.

The same institution encourages cross-selling and incents staff to build relationships and account depth. The representative who opened the checking account and credit line also linked a savings account and a credit card to the checking account. The representative now receives credit for opening a checking account, savings account, credit line and a credit card. In addition to complaining about the credit line the consumer complains he or she did not need the credit card. The representative linked it to the account automatically and told the consumer to cut it up or not to use it if he or she didn't need it.

Testing checking account opening practices through mystery shopping will measure whether or not representatives are clearly explaining the role of the credit line and over draft protection and the rate and fee involved. In addition, it will detect the addition of accounts not needed by the customer. The bank can then take steps to ensure consumers are made aware of the terms and conditions associated with the credit line and over draft protection and ensure the customer only received accounts needed.

Home Equity Credit Lines and Unsecured Loans

Home equity credit lines, home equity loans and unsecured personal loans are sold through bank branches by representatives who sell many products including deposit and loan products and at times investment and insurance products. A secured home equity credit line or home equity loan might be offered to a home owner seeking funds for a home improvement and funds to pay off some debts. An unsecured loan might be offered to a consumer seeking cash to pay bills, take a vacation or even to a homeowner seeking funds for these purposes and improve the home.

Let's review a case where a customer seeks funds to improve the home and pay off debt and applies for a home equity credit line. The customer is approved, the loan is closed in 30 days and the customer has access to the funds in another 3 days. The customer is highly satisfied. However, after some time passes the home equity credit line customer finds his or her monthly payments have increased. The interest only period ended and the index upon which the rate is based also increased. In addition, the customer has been using the home equity line of credit to pay credit card bills and has not paid down the credit line to cover the credit card purchases. The home equity customer complains. He or she did not know the rate could change and that payments were interest only. In addition, he or she financed household good purchases against his or her home. The bank representative said a good feature of the home equity credit line is that it can be used to pay credit card bills. The customer claims if he or she had known, a fixed rate home equity loan would have been opened.

And what about the Hispanic unsecured loan customer who learns someone else, a non-Hispanic white, took out a similar loan for about the same amount of money at the same time and is paying less interest. It turns out the bank representatives have some discretion in the rate charged. The representative did not exercise flexibility when quoting the rate to the Hispanic customer and the Hispanic customer did not negotiate. The Hispanic customer now complains and alleges discrimination..

By testing or monitoring the sales process through mystery shopping the financial institution could have identified the extent to which its representatives are informing potential home equity customers about the features of the home equity line of credit and whether the line of credit was compared to a fixed rate loan. In the case of the unsecured loan the bank can identify inconsistency in how representatives are quoting rates and terns to potential customers. The bank can take action to correct these issues, limit risk and prevent violations of consumer protection laws. Importantly, the bank takes the added step of ensuring the testing program qualifies for the self testing privilege under ECOA and conducts the testing under attorney client privilege with the specific purpose of measuring adherence to ECOA. By making use of the self testing privilege and attorney client privilege the results are not subject to disclosure and cannot be used against the financial institution by third parties suing the institution.

Prepaid Cards

More financial institutions are offering prepaid cards. The cards are increasingly sold through retail stores and the web to the unbanked and those unable to secure a credit card. Terms and conditions are often included on and inside the package containing the card or via the internet.

It's not uncommon for an unbanked consumer to notice a prepaid card display when shopping in his or her local drug store. The consumer acquires the card and is highly satisfied. The card will help the consumer manage his or her budget, avoid over draft fees and provide a mechanism to pay for goods and services while he/she or he rehabilitates credit. After a couple of months however, the consumer finds he or she does not have the all the funds deposited on the card less purchases. There was an acquisition fee, a monthly fee, a fee to reload the card and a balance inquiry fee. There was also an ATM fee when a withdrawal was made at an ATM. The customer complains. The customer wasn't aware of all the fees. If the customer knew about the fees it would not have been purchased. Were terms and conditions on the packaging in a place where they could be reviewed prior to purchase? The customer says "I did not know about all the fees and many of the terms were not on the outside of the package and the terms on the package were not clear."

Had the bank that provides the funds to the company marketing the pre paid cards arranged for mystery shoppers to visit a sample of stores to monitor retail and merchandising conditions, purchase the prepaid card and send the card and packaging to the financial institution it could have assessed the risk regarding the cards in store marketing, including its packaging and how the terms are disclosed to consumers. In addition, interviews or focus groups with card purchasers could have detected concerns and enabled the financial institution to evaluate and propose changes to the packaging so the fees and terms could be reviewed prior to purchase.

Reverse Mortgages and Annuities

Most financial institutions offer non-deposit investment products and some offer reverse mortgages. Unlike bank deposits, investments are not covered by FDIC insurance, are not guaranteed by the bank and involve risk to principal. Many bank customers are older and conservative and especially receptive to sales and marketing activities that offer higher returns while deemphasizing the potential loss to principal.

Critical Steps for Self Testing

- Develop a clear objective,
- Choose the methodology and number of evaluations,
- Set action standards for decision making,
- Develop an easy to understand and bias fee questionnaire,
- Select an analytical approach that satisfies the objective,
- Establish protocols to ensure the program is conducted under attorney client privilege and/or satisfies the requirements for the self testing privilege, and
- Put in place an action plan

Let's take the example of a female customer, 70 years of age with a certificate of deposit that just matured who asks the bank representative if there is a way she can earn more on her money. The representative recommends an annuity as a good alternative and refers her to a representative at the branch who is authorized to sell investments and insurance products. The representative informs the customer that she can earn more than a CD in a variable annuity and the annuity will pay her a lifetime income. The customer uses the money from the certificate of deposit to enroll in the annuity. At the same time the representative suggests a reverse mortgage and counseling to the customer. The customer goes to counseling and decides the reverse mortgage is a good way to afford her home, pay for home repairs, and feel financially secure. The customer is highly satisfied.

A few years pass and the customer and her children review her annuity statement and notice the fee charged and that her money is now worth less than the funds she had from the CD that matured. The customer complains. In addition, the woman's health has deteriorated and she has moved into an assisted living facility. The bank is now asking for repayment of the loan. The customer's children now complain. She thought the funds were secure. She was told by the bank representative that an annuity was a good alternative. She didn't understand they were dependent on the underlying investments. In addition, she didn't know if she moved or wasn't living in her home the loan would come due. She feels misled.

Testing the referral and investment and reverse mortgage sales processes through mystery shopping can help the bank detect practices which might confuse and mislead customers. The mystery shopping program can also monitor adherence to inter-agency guidelines concerning the sale of investment products. Had the bank implemented this program it could have detected that bank representatives were recommending investment products and that investment specialists were not informing potential customers about the nature of investment products and the risk involved. In addition, the bank could have detected the offering of reverse mortgages and measured whether the features or terms of the reverse mortgage were being adequately explained. Based on this information it could have taken action to change practices and help ensure customers understand the differences between deposit products and investment products and the nature and terms of reverse mortgages.

Self testing, matched pair testing and post application consumer surveys can help financial institutions manage risk in this new age of compliance. Being proactive and adopting a culture of fair and equitable customer treatment will help a financial institution navigate the complex web of government oversight and regulations while fostering high levels of customer loyalty and customer satisfaction.