

CONCEPTUAL FRAMEWORK

CONSUMER PROTECTION IN THE AREA OF FINANCIAL SERVICES, PROVISION OF FINANCIAL EDUCATION AND REGULATION OF MEDIATORY AND ADVISORY ACTIVITIES IN THE FINANCIAL MARKET

Submission Report

The Programme Statement of the Government of the Slovak Republic from August 2006, Chapter 2.1 Macroeconomic Framework, Public Finance and Taxes, Section: Financial Market and Protection of its Participants, amongst other matters, states the following:

"The Government shall assure appropriate protection of participants in the financial market focusing on the appropriate protection of non-professional investors and depositors against a possible failure of financial market subjects and shall strengthen prevention in this area. The Government will, therefore, propose measures in order to equalize the position of these clients and their greater awareness of products as well as the related fees. With regard to this, the Government will devote special attention to supporting the long-term financial education of the general public. The Government will also support activities that will render more efficient the system of compensation for non-accessible deposits and client's investment assets.

The Government shall review and systematically adjust the manner of financial and investment services mediation as well as the rules for the provision of financial consulting."

In this conceptual document, the Ministry of Finance of the Slovak Republic submits its intention as to which approach, methods and measures it intends to use to fulfil the above-cited part of its Programme Statement.

Complex realisation of this intention consists of appropriate provisions and changes which require implementation in three interrelated areas: increasing consumer protection in the financial market; increasing the level of financial education and general financial enlightenment; and adapting the legislation relating to financial services and products mediation and financial consulting.

1. INTRODUCTION

The number of financial services providers and intermediaries has increased rapidly during recent years together with the continually growing complexity and diversity of financial market tools. This is the result not only of the consistent liberalisation of business in the financial market but also of the ease of provision of cross-border financial services after the Slovak Republic's accession to the European Union.

The new legal and business environment ushered in favourable conditions for legal and natural entities, operating professionally in the financial market in the areas which are consistently regulated and supervised, to realise their professional activities. Thanks to significant economic growth and increasing consumer domestic income, the volume of disposable short- and long-term financial funds which consumers are willing to entrust to professional financial institutions is increasing. Consumers are more frequently forced to decide on the utilisation of their current and often also future incomes. Their decision-making is strongly influenced by sophisticated promotions on the part of financial institutions and their intermediaries but the consumer lacks confidence that his/her final decision on the utilisation of his/her funds was rational and supported by sufficient knowledge on the subject.

This situation is caused by a fundamental information and professional asymmetry in the financial market - the supply is created by financial institutions and their intermediaries, i.e. persons usually possessing the appropriate professional competence and financial education whose activities are further supported by sophisticated forms and methods of sales, but the demand for financial services consists not only of professional investors but also of a large group of non-professional users that are readily influenced and vulnerable because their knowledge of financial market operations and different services is not adequate for making qualified and rationally independent decisions.

Although a large sector of the population is not professionally capable in the financial area, they are exposed on an almost daily basis to the need to use the services of financial institutions, which may range from deposits and withdrawals in banks up to consumer loans or other forms of investment or insurance activities. Although the primary responsibility for disposing of own assets will always rest with the citizen alone, we cannot fairly expect from him/her an understanding of the complex financial markets at a level commensurate with that of professionals.

This highlights the growing need for adopting measures that will lead to greater consumer protection in the provision of financial services. These should, in the main, be measures leading to greater awareness and financial literacy on the part of the consumer as well as greater transparency in the mediation of financial services. The aim is to strengthen the prevention before any failure of participants in the financial market that could lead to damage to the property of an inadequately informed or duped consumer. Within the financial services consumer protection, it is also desirable to create an effective mechanism for the out-of-court resolution of disputes between consumers and financial services providers.

Complex realisation of this intention consists of appropriate measures and changes in the following three areas:

1. Increased consumer protection in the financial market - in this area it is especially necessary to:

- a) increase and improve the provision of client information on the part of financial institutions with regard to their services, as well as to make the rules for their promotion more precise and to prevent misleading and deceptive advertising,
- b) review the legal options available to a consumer for defending his/her rights resulting from contractual relations with financial services providers and intermediaries and ultimately to modify an institutional framework for enforcing consumer rights focusing on the creation of an effective mechanism for out-of-court settlements.

2. Increasing the level of financial education and general financial enlightenment - in this area it is especially necessary to:

- a) increase the overall awareness of the population with regard to the financial market, focusing on ensuring the long-term financial education for the financial public with participation in financial institutions, academia, government authorities as well as supervisory bodies,
- b) create conditions for the regulation of certified financial education in order to ensure that those persons licensed to perform activities on the financial market are equipped with the appropriate specialised skills.

3. Modification of regulation in the area of financial services intermediation and financial consulting – in this area it is especially necessary to:

- a) unify the conditions for financial services intermediation and financial consulting provision in the whole financial market,
- b) refine the rules for the activities of each financial intermediary and advisor in relation to clients, to improve enforcement of adherence to these rules and business ethics of advisory and intermediary subjects.

Realisation of the intentions stated in this conceptual document will require further legislative as well as institutional changes and measures. The responsible authorities are to ensure that these changes are discussed with the professional public.

While adhering to the usual procedures and methods, the fulfilment of the basic intentions stated in this conceptual framework should be possible approximately within a two year horizon.

2. CONSUMER PROTECTION IN THE AREA OF FINANCIAL SERVICES

Almost every citizen currently encounters the services of financial market institutions. In the most basic case, he/she has a current or deposit account in a bank and citizens increasingly frequently use payment or credit cards for payment of their purchases or have a consumer loan or mortgage.

The more complex and sophisticated the services and products of businesses become, the more difficult it becomes to protect either the transparency of the business environment and the propriety of the economic competition or consumer rights. This is especially valid for doing business and providing services in the financial market as, in many cases, financial institutions handle almost the whole current or future property or income of their clients.

The protection of business in the financial market in the Slovak Republic is at a standard European level. A functional and efficient supervision over financial market activities has steadily been built up over recent years and its integration into one supervisory institution (the National Bank of Slovakia) was completed in 2006. In accordance with valid legislation, the supervision contributes to the financial market stability and its healthy and safe operations.

The issue of consumer rights protection in the area of financial services is more complex – especially in the area of financial institutions' clients who do not receive financial services within their business or as other remuneratory activities but as non-professional consumers - non-enterprises.

We can evaluate positively the fact that the legal framework of the Slovak financial market, in accordance with the law of the European Communities, provides relatively complex protection of the handling of the assets of depositors as well as client assets of investors. The law also requires fulfilment of the duties of information and notification of the subjects in the financial market. Specific Acts also regulate the activities of financial institutions in relation to their clients. In the case of non-professional depositors and investors, institutions have been created for the purpose of the provision of compensation for non-accessible deposits received by credit institutions (Deposits Protection Fund) or for non-accessible client assets received by companies providing investment services (Investments Guarantee Fund). Supervision of all the above activities and institutions is wholly within the competencies of the National Bank of Slovakia.

However, in the relations between financial institutions and their clients, there are also areas which the consumer public perceives to be non-transparent and more favourable to financial institutions. As a financial services provider almost invariably has superiority in terms of information, as well as professional and legal dominance, an unprotected consumer gets into a disadvantaged position by insufficient transparency and weaker enforcement of the law.

Those subjects offering financial services to the public that do not require specific permission from the financial market supervisory body form a particular group. These are services that are neither specifically regulated nor supervised and they are usually offered by non-banking subjects such as consumer finance companies, leasing companies, companies providing loans, etc.

The interest payments, along with the hidden costs of the financial service, can be significantly higher in the utilisation of services from these companies than in a comparable banking transaction. Some companies provide consumers with their own debit cards for a

purpose-built use where they provide a non-cash loan up to the amount of SKK 50,000 per 24 months while the annual interest rate, excluding costs for account administration, drawing of statements and other transactional fees, is often higher than 25%. Citizens have even bigger problems with companies providing overpriced cash loans for inappropriately high interest rates. These are often amounts below SKK 10,000 with an interest rate reaching almost up to 100% on an annual basis. The clients of these companies are frequently citizens who have objectively more difficult access to bank loans, either because of their inadequate knowledge of banking and their related reduced ability to arrange a loan or because the more cautious banks would not provide them with a loan due to their high indebtedness.

Consumer awareness of financial services and their promotion

The consumer public's level of information of individual financial services and the option to compare their benefits and the costs incurred by a consumer when receiving such services is a frequently discussed topic.

The fact that, from July 2006, it has been possible to discover the amount of fees charged by individual banks, subsidiaries of foreign banks and building saving banks¹ for standardised banking transactions on the internet site of the National Bank of Slovakia has been quite favourably received. Consumers are now able to get the information which they would otherwise need to track down on the internet sites of individual financial institutions or they would need to use the advice of financial specialists in one location. The option to compare the fees of individual banks in cases of comparable services is also a significant effect that creates competitive pressure on those banks with higher prices. Taking into consideration the relatively low internet penetration in consumer households (compared to the EU average), this option of banking fees comparison is currently available only to a small group of more advanced consumers.

A systematic comparison of the costs entailed in the provision of financial services in other sectors of the financial market is still lacking². Comparisons of non-life and life insurance or collective investment parameters appear in the press with higher or lower periodicity but there is no legal act imposing a duty to publish this information on a regular basis on any authority. Internet portals systematically mapping and comparing the financial products and services of individual institutions exist in several European countries. These portals are often operated by professional consumer protection associations but also by government authorities or supervisory bodies³.

Another area which is not perceived very positively is the promotion of financial services. Rules for the promotion of services are precisely and strictly defined in some financial market segments⁴. For example, the Act binds companies administering mutual or pension funds to provide notice in the promotion of their services that there is a risk associated with the investment and that previous earnings are no guarantee of future earnings. In the case of consumer loans, there is also a duty to state the annual percentage cost rate linked with the

¹ A duty to submit information on fees required from a client to the National Bank of Slovakia for the above stated institutions given by the provision of § 37, par. 3 Act No. 483/2001 Coll., on Banks as later amended .

² The area of retirement pension savings forms an exception as pension administration companies are obliged to regularly publish selected information on fees for pension funds administration and these data are regularly published in periodicals summarily for the whole sector.

³ An internet portal www.moneymadeclear.fsa.gov.uk which is operated by a British authority supervising the financial market (Financial Services Authority) can be cited as an example.

⁴ For example, in the area of collective investment or retirement pension savings.

service. But some companies exploit the non-existence of precise rules in promoting their services and they provide scarcely verifiable or deceptive facts or information creating deceptive impressions of the real benefits of the service. Summarising earnings over the full period of duration instead of earnings on an annual basis can be mentioned as an example.

Consumer protection in disputes resulting from contractual relations with financial institution

Specific Acts on the financial market explicitly state in their provisions that disputes resulting from contractual relations between the subjects of banking, capital market, insurance or pension savings and the persons to which these subjects provide their services whose proceedings and decision-making pertain to appropriate courts or other authorities are not subject to the supervision of the financial market carried out by the National Bank of Slovakia.⁵ In this connection, specific Acts mostly refers to the Civil Procedure Code⁶.

In reality, this means that a client of a financial institution who feels to have been harmed by the institution can defend these rights only through tort litigation. This is the most usual means for the resolution of disputes among private subjects and it is usually not linked to the fulfilment of other restricting conditions.

However, due to the overloading of our judicial institutions and because of the generally demanding and complex topic of financial law, any dispute can extend over an extremely long period, while it is possible that the client cannot use his/her property which he/she entrusted to a financial institution up to the time of the dispute's resolution. Taking into consideration that, for a qualified decision on justifying the consumer's complaint, it is not only necessary to know the whole complex legal financial market framework but also to have appropriate knowledge on the operation of the financial market and its individual services, it can prove very demanding to achieve justice.

But legal Acts of the European Communities⁷ require the provision of fast, efficient and effective settlement of disputes between clients and financial institutions and this also by out-of-court settlements. The gradual implementation of these provisions into directives related to financial services is a trend which will also continue into the future in the case of European financial law.

In many European countries, there are specific ombudsman institutions whose activities are focused on consumer protection in the area of financial services and which, in many cases, serve for out-of-court dispute settlements between companies providing financial services and their clients, too. In addition to this function, these institutions also serve as prevention bodies – they can usually inform the appropriate financial institutions as to errors in their activities

⁵ E.g. § 6, par. 2 of Act No. 483/2001 Coll. on Banks, as later amended, § 136, par. 1 of Act No. 566/2001 Coll. on Securities and Investment Services (Act on Securities) as later amended, § 99, par. 3 of Act No. 594/2003 Coll. on Collective Investment as later amended, § 42, par. 4 of Act No. 95/2002 Coll. on Insurance as later amended, § 114, par. 3 of Act No. 43/2004 Coll. on Retirement Pension Savings as later amended, § 70, par. 3 of Act No. 650/2004 Coll. on Supplementary Pension Savings as later amended.

⁶ Act No. 99/1963 Coll. Civil Procedure Code as later amended.

⁷ Article 10 of European Parliament and Council Directive 97/5/EC on Cross-Border Credit Transfers.

Article 14 of European Parliament and Council Directive 2002/65/EC on Distance Marketing of Consumer Financial Services.

Article 11 of European Parliament and Council Directive 2002/92/EC on Insurance Mediation.

Article 65 of European Parliament and Council Directive 2004/39/EC on Markets in Financial Instruments.

and they can cooperate with the supervisory bodies or authorities appropriate for proceedings in criminal law issues by defining the deficiencies. In order to ensure law enforcement, ombudsman institutions are entitled to initiate proceedings and impose sanctions against financial institutions.

Binding legal Acts of the European Communities do not amend the details related to an internal organisation and the operation of such institutions. The specific shape of these institutions is, therefore, not unified and it is strongly influenced by the various institutional specifics and historical traditions of the country in question. In principle, it is possible to identify two basic models –these are either the institutions for out-of-court disputes settlement established by the state (law, government, etc.) as government or public authorities or as a part of bodies having supervisory powers over the financial market established or recognized by the government or these are mechanisms for out-of-court disputes settlement linked to associations or professional chambers of financial services providers. When the supervision over the banking sector or over the whole financial market is incorporated into a central bank, the institution ensuring out-of-court disputes settlement is usually established outside the supervisory body which eliminates some potential conflicts between the protection of consumer interests and ensuring financial sector stability.

Effective institutions for out-of-court disputes settlement established by government are, for example, in the United Kingdom (Financial Ombudsman Service), Ireland (Financial Services Ombudsman, Pensions Ombudsman) or in Sweden (Allmänna Reklamationsnämnden - National Board for Consumer Complaints). In some cases, there is a supervisory body or an ombudsman by a supervisory body entitled to settlement of disputes, e. g. in Luxembourg (Commission de Surveillance de Secteur Financier), France (Médiateur de l'Autorité des Marchés Financiers) or on Malta (The Consumer Complaints Manager at the Malta Financial Services Authority).

By this method of organisation, the activity of such an institution is usually regulated by an Act and executing regulations. By implementation of this model, the institution of financial ombudsman can be either a direct government body or an independent legal entity with a significant government influence. In some countries, the decisions of a financial ombudsman are legally binding; in others he/she only has the authority to initiate legal procedures and his/her decisions have only a recommendatory character.

In European countries where institutions for out-of-court disputes settlement are linked to professional associations or chambers, this model has usually been developed historically and the operation of these institutions is usually not regulated by legal Acts. As examples, the following may be mentioned: Germany (Ombudsman by Federal Union of German Banks), Austria (Common Council for Arbitration Procedures of Austrian Credit Institutions) or Italy (Banking Ombudsman by Italian Association of Banks). The decisions of a financial ombudsman are not legally binding in these cases but financial services providers which are members of the appropriate professional associations respect them on a voluntary basis; ultimately the obligation to respect such decisions results from their membership in the association. By implementation of this model, there are usually specific institutions for out-of-court disputes resolution for individual sectors of the financial market, while credit institutions and insurance companies are traditionally represented most frequently.

In the Slovak Republic, the topic of out-of-court disputes settlement is institutionally covered only in the area of system of payments and some other disputes with financial institutions in the banking industry. With effect from July 1st, 2003, a Permanent Arbitration Court of the

Slovak Banking Association was established which decides in two chambers on disputes resulting from the system of payments and disputes from commercial and civil relations. Activities of this arbitration court are financed by annual contributions from the executing institutions and issuers of electronic payment means.

The institution of ombudsman was established in the Slovak Republic by Act No. 564/2001 Coll. on Ombudsman but its scope covers only public administration bodies, territorial self-government bodies and legal and natural entities which decide on the rights and obligations of natural and legal entities in the area of public administration, or otherwise influence the rights and obligations of legal and natural entities in the area of public administration according to a specific Act. Out-of-court settlement of disputes is regulated by Act No. 420/2004 Coll. on Mediation and on amendments to certain Acts in the Slovak Republic. This Act covers disputes resulting from civil relations, family relations, business liability relations and labour relations.

Some legal Acts connected with consumer protection in the area of financial services

The current legal framework related to consumer protection in the area of financial services in the Slovak Republic, including services provided by non-supervised subjects, contains, besides general Acts (in particular, the Commercial Code) the following legal Acts:

Act No. 258/2001 Coll. on Consumer Loans which regulates some conditions of consumer loans provision, terms and conditions of the contract on consumer loan, calculation of total costs for a consumer connected with the provision of a consumer loan as well as other provisions related to consumer protection also in relation to subjects which do not come under the supervision of the National Bank of Slovakia. In accordance with this Act, the contract on a consumer loan has to contain an annual percentage rate of costs (RPMN) calculated according to a mathematical formula in addition to the general provisions. This rate represents the total costs for a consumer (i.e. all the costs, including interest and fees, which are connected with the provision of a consumer loan) expressed in the form of an annual percentage share of the value of the loan provided. The Act further states that, if the value of RPMN is not stated in the contract, the consumer loan is deemed to be interest-free and free-of-charge.

Act No. 147/2001 Coll. on Advertising which defines advertising as the presentation of products in a particular form with the aim of putting them on the market while the product is represented by a merchandise, service, real estate, business name, trademark, indication of product origin and other rights and liabilities connected to business. A disseminator of advertising is each natural or legal entity which disseminates an advertisement within its business activities. Advertising has to be in accordance with the rules of economic competition and good manners. Advertising may not be deceptive and hidden. These provisions also relate to the provision of financial services, regardless of whether the providers are supervised or non-supervised subjects operating in the financial market.

Act No. 266/2005 Coll. on Consumer Protection by Distance Financial Services and on the change and amendment of some Acts covers consumer protection by financial services provided by the supplier through means of distance communication on the basis of a distance contract and closing of a distance contract.

Solutions proposed for the given area

- 2.1 A legal Act with the scope of powers for the whole financial market including non-supervised financial institutions will set out common rules regulating the activities of financial institutions and financial intermediaries in relation to the consumer by the provision and mediation of financial services and by their promotion. (However, there is no intention to touch the existing legal regulation related to supervised financial institutions in accordance with specific Acts.) The subject of legal regulation will be, in particular:
 - a) rules for the financial institution's activities related to contact with the consumer of financial services respecting the rules of fair business with professional care in the interest of the consumer,
 - b) the extent of the minimum duties of information of subjects providing financial services,
 - c) rules for the promotion of financial services focusing on determining acceptable or non-acceptable forms of promotion, the prohibition of deceptive and non-ethical advertising,
 - d) the manner of supervision over adherence to the provisions of this legal Act and sanctions for its violation.

- 2.2 The creation of an internet portal for financial services and financial enlightenment will be confirmed. The portal could be a part of the central public administration portal where the following information would be published and regularly updated in a transparent and user-friendly way:
 - a) information on financial services provided and the costs connected to their utilisation with the possibility to compare the appropriacy or inappropriacy of the service in question through comparison with similar services of competitor companies or through the simple modelling of potential situations e. g. by utilisation of a financial calculator,
 - b) basic information on the financial market and financial services with the aim to focus on basic financial enlightenment in this area.

- 2.3 The best model for an institutional framework ensuring consumer rights protection in the area of financial services by resolution of disputes resulting from contractual relations with a financial institution, and by resolution of disputes resulting from the creation of contractual relations on the basis of an inappropriate recommendation of a financial services provider or intermediary on a basis of a deceptive form of promotion, will be discussed and accepted in a professional discussion. The following prerequisites should be met:
 - a) out-of-court disputes resolution will be ensured which will be legally binding on the disputing parties and the appropriate resolution will represent an execution entitlement;

- b) this method of disputes settlement will be an efficient and significantly cheaper alternative compared to disputes resolution before the court; each of the parties will retain the right to seek his/her rights in the court proceedings,
- c) the relation between the form of the out-of-court settlement and dispute resolution before the court will be more precisely defined, as well as the group of persons entitled to request an out-of-court resolution;
- d) issues related to organisation, activities and financing of the institution will be taken into consideration;
- e) when searching for a suitable institutional model, positive experiences from other European countries will be used in the creation and operation of ombudsman institutions.

3. FINANCIAL EDUCATION

The importance of financial education has increased in recent years, in particular as a result of developments in the financial market and demographic, economic and strategic changes. The financial markets have become more sophisticated and they continue to offer more and more sophisticated services, many of them designated only for a narrow target group. Currently, consumers have better access to a whole range of credit and saving structures which differ with regard to fees, interest rates, maturity or other parameters. And it is certainly not easy for the consumer to evaluate the quality of these structures or to compare them. This is especially difficult in the case of long-term financial services – e. g. the quality of life insurance will be revealed only after attaining a certain age or in the event of an insurance claim.

As a result of the changes in the pension insurance system, more and more employees are taking responsibility for their own pension savings. Taking increased life expectancy into consideration, individuals wish to ensure that they have sufficient savings to cover their needs in their retirement. The gradual decrease in the proportion of the active population creating resources for the continuous financing of pensions leads to seeking an alternative way of saving and investing aimed at assuring pension incomes and increasing the responsibility of individuals for their future incomes.

This development leads to important decisions, particularly for three social categories: those people saving or investing for a pension, those in receipt of credits and loans including credit card users, and those utilising the services of instalment companies. An appropriate financial literacy is a very important factor in supporting qualified decision-making for these consumers along with a good financial advisor and high quality consumer rights protection system.

Since 2005 there has been an extensive programme focused on improvement of financial education within the Organisation for Economic Cooperation and Development (OECD). Based on an international analysis of the level of financial education and a comparison of financial education programmes and their efficiency⁸, the OECD finds that the financial literacy of the population is not at an adequate level even in economically developed countries⁹ and it highlights that economic, demographic and political changes in the world require the governments of individual countries to devote greater attention to financial education of population¹⁰.

The OECD analysis underlines the importance of long-term financial education for the population. Governments should explain to their citizens that financial education is not solely the preserve of investors but also pertains to every family which wishes to pay for accommodation, education for children and pensions for parents. Besides this, it is necessary

⁸ Improving Financial Literacy – Analysis of Issues and Policies. Paris, OECD, 2005. 181 pages.

⁹ In Japan 57% of the population do not understand the general functions of financial products, 71 % do not know how to use shares and bonds and 29% do not even know anything about life insurance and pension plans; in USA 25 % of employees do not save for their pension and in Australia 67% of the respondents claimed to understand compound interest but, after submitting an actual example, only 28% understood it.

¹⁰ With reference to OECD member countries, high attention to financial education at government level is devoted especially in USA, Canada, Japan, Australia, New Zealand and in several EU member countries. Governments have established institutions supporting financial education in some countries (e.g. Financial Literacy Foundation established by the Government of the Australian Union).

to understand that people at different stages of their lives need different types of financial products and educational programmes need to respond to this. The information in programmes needs to be formulated simply and comprehensibly, programmes need to be focused in particular on basic issues like savings, loans, insurance, pension insurance and investments. A financial education programme should employ the forms of a national campaign, special internet sites, charge-free information services and charge-free access to special electronic documents and manuals through digital or virtual libraries.

Financial education

Financial education¹¹ is a process whereby consumers of financial services and financial investors enhance their knowledge of financial products and concepts and, through information, training or objective consulting, develop their experience and confidence in order to attain greater awareness of financial risk and opportunities so as to be able to make informed decisions, to know where to search for help, and to be able to take other effective steps to enhance their financial welfare.

It is necessary to differentiate between financial education and protection of a financial services consumer, although there is a certain overlap in these two categories. They have the provision of financial information in common but, where financial education is concerned, the consumer receives this information through training and advice while, in the case of consumer protection concept implementation, a duty is imposed directly on financial institutions through a legislative and regulation framework to provide their clients with essential standard information, or legal protection is ensured for the consumer in the event of a failure in the relation between a consumer and financial institution.

We can simply say that an institutional framework for consumer protection represents a certain social safety net for consumers who are unable or unwilling to undergo financial education and thereby gain or improve the level of their financial literacy. In general, we can say that citizens with lower levels of education and some minority groups or citizens with lower incomes possess lower levels of financial literacy.

Financial literacy

Financial literacy entails the ability to make professionally qualified judgements and effective decisions on the utilisation and administration of financial resources. It is becoming a prerequisite for existence in a modern society and it is more and more important for the sustainable welfare of individuals and of the whole of society.

All age and income groups can benefit from greater financial literacy. For school graduates just entering the labour market it provides basic financial education, simple tools for budgeting personal finances and it will support them in achieving a better balance between their savings and debts. Financial literacy enables families to maintain a higher financial discipline through savings to assure accommodation and education for them and their children. Education enables employees in their middle and later age to make reasonable investment decisions whether in relation to their pension savings or by increasing their financial wealth. Financial education enables low-income groups to avoid products and services with high fees. Greater financial knowledge will enable groups with disposable financial resources to not

¹¹ The definition of financial education stated here is adapted from the cited OECD study.

only better understand more complex solutions but also to better evaluate the level of their risk.

Financially educated consumers of financial services can influence the market and by this also its economy. In the demand for services that better suit their needs, they create pressure on service providers to adapt their products and services and, through increasing competition, also on quality improvement. It is probable that consumers with financial education will have a greater commitment to saving. Growth in the savings rate, together with growing financial literacy, positively influences the amount of investments as well as economic growth. What is more, consumers with a better financial education are more able to protect themselves against potential errors in the activities of financial institutions but also to inform the supervisory body on any such violation of the rules for supervised subject activities. Finally, these actions lead to more rapid remediation of defects in the activities of supervised subjects than by the execution of supervision at the initiative of a supervisory body.

Increasing specialised skills for performing intermediary, advisory and other specialist activities in the financial market

Besides the gradual creation of programmes and projects to ensure the financial education of the general public, it is also important to direct greater attention to improvement of the financial knowledge of persons who are or can be, in the sense of the relevant legal Acts, specialised for the execution of licensed activities on the financial market. For example, in the case of financial intermediaries who have to demonstrate a more than basic level of specialised skills for performing their activities, regular renewal of their specialist education is anticipated, as well as regular repeat testing of their specialist skills from the area of the financial market where they offer financial services and financial consulting.

In a group of independent financial advisors, the creation of an institution of an independent certified financial advisor is expected - a natural entity with a special *certified education* in the area of finance attained in a way regulated by law from an educational institution authorised to provide this kind of education.

Solutions proposed for the given area

3. 1 The most suitable model for the permanent provision of effective financial education for the public will be discussed and adopted in a specialist discussion. Meanwhile, it is necessary to consider the creation of a coordinating centre or institution, the task of which will be, among others, to:
 - a) methodically manage, direct and coordinate individual educational, financial and media institutions participating in financial education;
 - b) perform research into the financial literacy level and consumer needs in the area of increasing information on financial services;
 - c) participate in complementing or directly operating a national information portal focused on information relating to financial services;
 - d) lead and cooperate by managing media and other campaigns focused on selected areas by the provision of financial services;
 - e) incorporate private financial institutions into financial educational activity through suitable forms of participation in its costs and realisation;
 - f) cooperate in the creation of educational programmes for financial education in elementary and secondary schools.

3. 2 To suggest the creation of an educational institution or a system (coordinated network) of educational institutions, the aim of which will be to assure:
 - a) continuous education and enhancement of the financial knowledge of persons who have or can have, in the sense of the relevant legal Acts, specialist skills for the performance of licensed or registered activities on the financial market,
 - b) one-off or repeated tests of specialist skills for the performance of licensed or registered activities on the financial market,
 - c) special certified education in the area of finance as an essential prerequisite for obtaining a licence to act as a certified financial advisor.

4. UNIFIED AMENDMENT OF MEDIATION AND CONSULTING REGULATION IN THE FINANCIAL MARKET

Contractual relations on the basis of which financial services are provided may be established by consumers either through direct contact with the financial institution which provides the services or through persons authorised to perform intermediary and consulting services in individual areas of the financial market.

Direct contact of a consumer with a financial institution is usual in the case of banking transactions (such as the administration of current or saving accounts, provision of loans, etc.) By contrast, there are some areas where the utilisation of the services of financial intermediaries traditionally predominates – it is very common e.g. in the case of insurance mediation, in the mediation of investment services, as well as in the mediation of pension savings.

Financial intermediaries and persons providing advisory services in various areas of the financial market together with front-office employees of “rock-solid” financial institutions are the persons who, by their direct contact with a consumer, are most able to influence his/her financial decision-making. Their professional level, communicative ability and ability to provide appropriate advice in the selection of a financial service significantly influence complex public opinion of the financial market and the activities of its institutions.

As persons mediating financial services and providing specialised financial consulting can, by their activities in individual cases, influence the decision of a consumer so that he/she can suffer damage to his/her property, it is clear that appropriate specialised skills of intermediaries and advisers are essential for consumer protection. It is also necessary for the consumer to be appropriately protected against the professional failure of an intermediary.

Despite the fact that, with the growing complexity of financial tools and services, specialised legislation regulating activities in individual areas of the financial market is gradually being unified, the legal framework for intermediation and advisory activities in the financial market is still not unified, although in some financial market segments these activities show a high level of similarity.

Taking into consideration the specialities of intermediation activities in selected areas of the financial market, special legislation has been created for these areas. It has been gradually created by various levels of practice which have led to comparable properties of activities and their definitions in individual areas being solved by different approaches.

The performance of activities connected to the mediation of financial tools and services and provision of financial consulting is currently legally amended by specific Acts for the area of insurance and reinsurance¹², investment services¹³, complementary pension savings¹⁴, and up

¹² Act No. 340/2005 Coll. on Mediation of Insurance and Mediation of Reinsurance and on change and amendment of some Acts as later amended and Announcement of the Ministry of Finance of the Slovak Republic No. 417/2005 Coll. as later amended.

¹³ § 61, par. 1 of Act No. 566/2001 Coll. on Securities and Investment Services and on change and amendment of some Acts (Act on Securities) as later amended and of the Ministry of Finance of the Slovak Republic No. 8/2002 Coll.

¹⁴ §§ 68 to 68c of Act No. 650/2004 Coll. on Complementary Pension Savings and on the change and amendment of some Acts as later amended.

to the end of 2006 the activities of intermediaries were also specifically regulated in the area of retirement pension savings.

In the individually mentioned cases, specific Acts define the conditions for granting the approval or registration of the appropriate intermediation activity and to what extent a financial advisor is authorised to provide financial consulting for a given area of the financial market. Financial mediation and financial consulting in other areas of the financial market are not legally regulated. The Slovak legal framework also lacks a general definition of financial mediation and financial consulting.

Therefore, it is necessary to create a legal framework for the common regulation of financial mediation and financial consulting in the Slovak financial market on the basis of the current legal framework for mediation and specialist consultation in selected areas of the financial market. A new legal framework should reflect the positive features and experiences from the current legal regulations and supervision over the activities of financial intermediaries, especially in the area of insurance and investment services.

Besides a definition of the concepts of “financial mediation” and “financial consulting”, a new legislative framework will also define the persons authorised for the performance of intermediary or advisory activities, the prerequisites for the performance of financial intermediary and financial advisor activities with a specific focus on specialised skills as well as on cases in which a licence for the execution of intermediary and advisory activities is necessary for commencement of the activity.

The intention is also to create the institution of a certified financial advisor as a financial advisor – a natural entity who has met the legally required specific assumptions for specialised skills including undergoing certified financial education.

A new legal framework should not touch the achieved status and quality of financial mediation and financial consulting in the areas of the financial market where there is a legal regulation which is harmonised with the law of the European Communities. The provisions of legal Acts representing a directive framework should, therefore, be special Acts in relation to the intended general legal framework.

In performing financial mediation or the provision of financial consulting, it is necessary for the client to be appropriately protected against the professional failure of the person providing the appropriate service on his/her behalf. Therefore, it is necessary to give special attention to the fact that procedures and rules should exist for financial intermediary (or financial advisory) activities determined by law in order to minimise the risk that, after the provision of professional care by an intermediary or consultant, the mediated financial services will not be suited to the given person or will not relate to his/her financial or personal possibilities or circumstances.

The Act will also determine the subject and extent of the supervision over the activities of financial intermediaries and financial advisors performed by the National Bank of Slovakia.¹⁵

¹⁵ Issues of unified amendment of financial mediation and financial consulting regulation were consulted with a specialist department of the National Bank of Slovakia. The text of this part of the conceptual framework was also created on the basis of this consultation.

Solutions proposed for the given area

4.1 A unified legal framework for financial mediation and financial consulting will be created in the financial market. The Act will:

- a) define the notions “financial mediation” and “financial consulting”;
- b) define the persons who may perform mediation and consulting activities;
- c) define the cases where a licence for the performance of mediation or advisory activity is a precondition for commencement of the activity of execution and those cases where only registration in the registry of financial intermediaries is sufficient; at the same time the Act will determine the conditions for provision of the appropriate licence or for registration in the registry of intermediaries;
- d) define the basic conditions for the performance of financial intermediary or financial advisor activities with a special emphasis on the specialist skills of these persons - these will be dependent on the type and extent of the activity and will be separated into several levels, while the Act will determine the conditions for achieving individual levels of specialised skills, especially the requisite education and length of experience in the area where financial mediation or financial consulting should be performed and also the opportunity to replace an inadequate education by a specialised test;
- e) determine procedures and rules for financial intermediary or financial consultant activities so that, after the provision of professional care by an intermediary or advisor, the risk that the mediated financial service will not be suitable for a given person or not appropriate to his/her financial or personal possibilities and circumstances is minimised – therefore the Act will determine rules for the performance of intermediary and advisory activities in relation to the client on the one part and on the other part it will determine the conditions for capital sufficiency and insurance of an intermediary for covering the liability for damages caused by performance of his/her activities;
- f) determine the subject and extent of the supervision over the activities of financial intermediaries and financial advisors;
- g) determine the relation of a general framework for financial mediation and consultation to specific regulations in these segments of the financial market where the reason for a specific adjustment will be the adoption of the European Communities law.

4.2 On the basis of specialised discussion, the regulation and supervision over specific types of intermediary and advisory subjects activities will be introduced or will be strengthened, while it is particularly necessary to consider:

- a) the creation of the institution of a certified financial advisor as a financial advisor – a natural entity who has met the legally required specific criteria for specialist skills including undertaking the certified financial education;
- b) regulation of multi-level networks of intermediaries;

- c) regulation of mediation of instalment sales companies and consumer finance companies services;
 - d) regulation of the mediation and provision of financial services whose underlying assets are specifically non-regulated investments with a higher level of risk which are not and should not be covered by the investment protection system, and which are dedicated only for qualified investors on the basis of a private offer (management of private risk assets).
- 4.3 On the basis of a specialist discussion, the option to introduce a shared regulation of financial intermediaries activities where some regulatory activities in relation to intermediaries of lower levels could be delegated to an accredited professional chamber with effective authorities to enforce the fulfilment of rules determined by this chamber; the activities of this association would be accredited and supervised by the National Bank of Slovakia.