Industry Canada Industrie Canada

Office of Consumer Affairs

Consumer Impact Assessment

Assessing how proposed policies may impact consumers

Canada

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Why assess impacts on consumers?

Understanding consumer impacts is critical to the success of public policies. Consumers not only benefit from competition, but also drive it, directly impacting on the competitiveness of firms and the productivity of a nation. However, consumers can also bear disproportionate risks and unintended consequences if expert analysis is not provided in the early stages when policies are being developed.

Traditional neo-classical economic models and microeconomic analysis generally focus on issues such as the cost of goods or services, their quality or availability, or other market phenomena. However, there is growing evidence that it is also important to take into account the limits of consumer rationality and self-interest, and the consumer's ability to access, absorb and analyze information, both of which affect how consumers make choices in the marketplace.

This guide encourages analysts to use a combination of traditional and emerging analytical approaches when assessing consumer impacts. It recommends they examine who the consumers are in the context of the proposal, the number of consumers who will be affected, the magnitude of the risks they face, and the implications of their making poor decisions. Supporting material and examples are provided below and in the appendices. The basic analytical framework is built around three key factors that are critical to assessing how consumers may benefit from, or be harmed by, new policies:

- anticipated market price and supply — how the policy will change prices, quality and supply of consumer goods and services;
- behavioural impacts — how the policy will affect business-consumer transactions and relationships, and how it will affect consumers' ability to make rational choices and thereby maximize their welfare and their influence on innovation and competitiveness; and
- distributional impacts — identifying which consumers will feel the greatest impact and how vulnerable and disadvantaged consumers may experience the change.

A broad range of information from a variety of sources can inform consumer impact analysis, particularly in areas that overlap with business and competition impact assessments. Examples include results obtained from using the various Treasury Board of Canada Secretariat cost-benefit and market impact assessment tools. This guide includes a brief section that sets out the importance and benefits of working directly with consumer groups. (See also Appendix B.)

The information in this guide is based on a research paper Industry Canada's Office of Consumer Affairs commissioned from independent policy consultant Dr. Derek Ireland, entitled *Methodology for Assessing the Consumer Impacts of New Regulations*. The guide also reflects input from Canadian consumer groups and provincial and territorial consumer protection agencies; however, it does not represent a consensus of these stakeholders.

A framework for assessing consumer impacts

Analysis of consumer impacts requires an understanding of the nature of consumer demand in an industry, insight into the effect the policy may have on consumer information, and knowledge as to how consumers may respond to complex products, services and transactions that the policy may help promote.

The following questions offer a framework to assist the analyst in the process of assessing consumer impacts.

1. Is the policy likely to lead to a significant change in the price and quantity of the product or service available in the market, or the quality and choice available to consumers?

This question looks at the impacts on consumers in terms of traditional economic factors, such as price, quantity and quality of the goods or services on offer in the market. Other issues worth examining which may indirectly impact consumers include:

- Will the policy stimulate or discourage innovation that could improve product quality or reduce prices, or the development of new products and services?
- Will it add to or reduce competition in specific markets over the short, medium and long term?

Standard economic theory predicts that new policies that reduce industry competitiveness and add substantially to business and industry costs will likely lead to higher consumer prices, reduced quantity of products and services and, perhaps, reduced quality and fewer choices for consumers. This would be particularly true in highly concentrated industries, since businesses facing little competition would likely pass on all or a significant portion of their increased costs to consumers.

The OECD's *Competition Assessment Toolkit* www.oecd.org and similar products developed by the Competition Bureau www.competitionbureau.gc.ca contain guidance that will be helpful when addressing these questions.

2. Is the policy likely to result in material changes to relationships between consumers and business?

With this second question, the analysis of the impact on consumers of new policies goes beyond the traditional areas of concern. It addresses changes in policies that may have an impact on interactions between consumers and business:

- Will the policy affect consumers' access to clear, concise and truthful information that allows them to realistically assess the value and usefulness of the product or service?

Knowledge of the industry and its track record in the areas of advertising and marketing will be particularly useful when assessing whether the information that industry provides to consumers is likely to be accurate, useful and helpful.

- Will the policy lead to situations in which suppliers may take undue advantage of consumers?

Research in the field of behavioural economics suggests that a number of factors beyond quality and price affect the decisions consumers make — that is, that consumers sometimes do not act as rationally as traditional economic theory would suggest. This makes it possible for suppliers to capitalize on the biases consumers have and the resulting mistakes they might make when assessing products and services. Appendix A contains descriptions and examples of two common consumer biases of importance to policy analysts when selecting, designing and assessing policy responses.

A word of caution: measures to mitigate any harm the new policy may create also need to be assessed, since they may have their own, unintended and negative side effects. For example, requiring suppliers to provide certain information about a product or service at the point of sale may lead to information overload for consumers, depending on the volume of information and the manner in which it is presented. This may result in consumers making less informed decisions, because they cannot, or will not, take the time to digest all the details. Moreover, suppliers may benefit because consumers may not consider all the factors related to their purchase, which otherwise may have led them to choose another product, service or supplier.

- Will it impede or diminish consumers' ability to seek redress when problems occur?

The industry's reputation for fairness and meeting its promises and obligations to consumers will provide insight into the potential consumer impacts of a new policy or regulation on the quality of the sales transaction and after sale service, including consumers' right to complain and be compensated in some way for poor products or bad service.

The OECD's *Consumer Policy Toolkit* (2010) www.oecd.org contains guidance that will be helpful when addressing these questions.

3. Is the new policy likely to have substantial negative impacts on vulnerable consumers and their interactions with business?

The response to this question brings together the results of the analysis prompted by the first two questions to assess whether the new policy would raise significant concerns related to the vulnerability of some or all consumers. It also addresses fairness and related issues that, in turn, would be expected to lead to significant consumer concerns and complaints, and place the effectiveness and fairness of the policy in significant doubt.

A few definitions will help set the context for this analysis.[1]

[1] Menzel Baker, Gentry and Rittenburg (2005) have attempted to define these concepts in *Building an Understanding of the Domain of Consumer Vulnerability*. The definitions here are from *What do we mean by vulnerable and disadvantaged consumers?* a discussion paper published by Consumer Affairs Victoria (Australia).

- **Consumer detriment** includes, in addition to any physical harm or monetary loss associated with the purchase, satisfaction less than a consumer's reasonable ex ante expectation or the denial of a transaction sought by a consumer.
- A **vulnerable consumer** is a person who is capable of readily or quickly suffering detriment in the process of consumption. A susceptibility to detriment may arise from either the characteristics of the market for a particular product, the product's qualities or the nature of the transaction; or the individual's attributes or circumstances which adversely affect consumer decision-making or the pursuit of redress for any detriment suffered; or a combination of these.
- A **disadvantaged consumer** is a person in persistent circumstances and/or with ongoing attributes which adversely affect consumption thereby causing a continuing susceptibility to detriment in consumption. As a result, a disadvantaged consumer repeatedly suffers consumer detriments or, alternatively expressed, consistently obtains below-average satisfaction from consumption.

All consumers can be vulnerable at one time or another. There are, however, more profound states of vulnerability in which a consumer is susceptible to particular disadvantage. This may occur, for example, when consumers live in poverty, have low financial or functional literacy skills, or live in geographically isolated communities.[2]

It is important to analyze the potential impacts of some policy proposals on vulnerable and disadvantaged consumers to ensure the initiative does not make it hard for them to buy critical goods and services such as food, financial and health services, energy, transportation, housing and education.[3] For instance, members of low-income households already often pay higher prices than those in other income brackets for tax preparation services, cars, car loans, car insurance, home loans, home insurance, furniture, appliances, electronics and groceries.[4]

Responses to this question would particularly utilize the policy analyst's prior knowledge of the industry in question and of past regulatory initiatives in this and similar industries in Canada and other countries. The responses would also benefit from the regulator's knowledge of the major proponent of the new policy or regulation, and a good knowledge of some of the key positions that Canadian consumer groups and other non-government organizations advocate.

[2] Sauvé, R. (2008). *Assessing Vulnerabilities of Low Income Consumers*, commissioned by the Office of Consumer Affairs, Industry Canada.
[3] Comité consultatif de lutte contre la pauvreté et l'exclusion sociale, *Planning, Aims and Objectives (2006-2009) Province of Quebec.*
[4] Brookings Institution (2006). *Poverty, Opportunity. Putting the market to work for lower income families.* See also, Caplovitz, D. (1967). *The Poor Pay More: Consumer Practices of Low-Income Families.*

Consulting Canadian consumer groups

In addition to using economic studies to support the above analysis, analysts should consider consulting consumers themselves. Public opinion research, surveys or focus groups of individual consumers can provide information to help them work through their assessment. Analysts may also want to search the Office of Consumer Affairs' ***Consumer Policy Research Data Base*** at www.ic.gc.ca/consumer/researchdatabase to find Canadian consumer research studies that may be relevant to their subject area.

There are also numerous consumer groups in Canada with expertise in a wide spectrum of subject matters. Engaging them early in the consultation process can ensure thorough evidence-based input. Appendix B contains a list of some of these consumer groups. Speaking with the head of any particular group about your policy proposal will give a sense of whether the group can provide the information required. Also be sure to check the group's website for the most up-to-date contact information.

Canadian consumers and consumer advocates are typically not well resourced, and will have a difficult time providing input if not given adequate lead time and resources to do their analysis and make recommendations. Departments and agencies should expect to cover the costs of research, travel, participation in focus groups, and other tasks they may wish consumer groups to carry out to help determine potential consumer impacts.

Making your organization receptive to consumer input

Making it easy for consumers to provide input as a matter of course and having processes in place to solicit it and integrate it into specific initiatives will help build rapport with consumers (groups or individuals) and enhance the quality of the feedback. Government policy managers may wish to ask the questions below about their operations and then make organizational or procedural changes in light of the responses.

Recognize the consumer interest

- Is there a clear view of who the consumer is in the organization's work, and how to define the consumer interest?
- Is there a process in place for identifying and tracking consumer issues?
- Are there clear channels through which consumers can communicate and raise issues with the organization?
- Is there regular liaison with consumer bodies, non-governmental organizations and academics to keep the organization informed about their issues and priorities?

Continually assess impacts on consumers

- Are there clear policies and procedures for dealing with consumer issues identified by tracking and consultation?
- Do business planning and risk assessment processes include consideration of consumer issues?
- Are there processes in place to ensure that the key consumer interest issues are explicitly explained, assessed, and addressed in policy and regulatory projects?

Maintain commitment at high levels

- Are there regular reports to senior management on consumer-related issues?
- Does management regularly benchmark the organization's processes against those of other organizations involved in consumer matters?[5]

[5] Adapted from the U.K Office of Communications, 2006, *Capturing the Consumer Interest, A Toolkit for Regulators and Government*.

CONCLUSION

Assessing consumer impacts using this guide can help ensure greater success and consumer acceptance of proposed policies and regulations. Analysts are invited to work through the questions in this guide, seek assistance from consumer groups where appropriate, and organize their offices to ensure greater receptivity to consumer input.

It is recognized, however, that there are situations in which qualitative or quantitative impacts simply cannot be calculated, or where legal and political imperatives give policy analysts and decision makers very little room to manoeuvre. In such cases, the information in this guide should be equally helpful in carrying out post-implementation analysis, and in allowing policy-makers to develop recommendations for appropriate adjustments, when needed, to mitigate unintended consumer harm.

Analysts may wish to contact the Office of Consumer Affairs (www.ic.gc.ca/consumer) for assistance in locating consumer research that is relevant to their subject area or to seek information about national and international consumer policy and research communities that may have information and tools available to help them with their consumer impact assessments.

APPENDIX A:
Behavioural economics in policy and regulatory development

Over the past two decades, academics in economics, psychology, sociology and game theory have been conducting research on how consumers actually think about and make decisions in the marketplace.

All market participants suffer to some degree from "bounded rationality" because of limited time, information, and/or computational and cognitive abilities. This leads to behavioural biases such as the use of rules of thumb ("heuristics") or routine habit to make decisions in the marketplace, which may lead in turn to mistakes. Market forces and consumer education can help to correct these mistakes. Nonetheless, these mistakes can have significant and lasting negative effects on market decisions and outcomes, and business and economic performance. They also prevent consumers from playing their full role in activating competition and innovation in the marketplace.

TWO IMPORTANT BEHAVIOURAL BIASES[1]

There are a number of behavioural biases that have been identified that have an impact on the way consumers make decisions. Two of the most important behavioural factors that analysts should be aware of when selecting, designing and assessing policy responses are: 1) how consumers may react to information and choice overload, and 2) how consumers may respond to various ways choice offerings are framed, and defaults are set.

1. Information and product choice overload (too much of a good thing)

For some products and markets, too many choices and overly complex offerings can be confusing and de-motivating. Consumers may put off a difficult decision, use a “rule of thumb” to reduce the number of choices, or stick with their current supplier for fear of making the wrong decision or because sorting it all out seems overwhelming.

Governments, independent consumer groups and other non-government organizations often provide policy responses to this situation by providing online calculators and other tools that help the consumer to wade through the complex and sometimes contradictory information. In other cases, very specific and simple disclosures tailored to an individual’s circumstances may be required to focus the consumer’s attention on key decision-making issues – for example, the long term cost of making a minimum payment on a credit card bill. Instruments such as these enable consumers to make more informed choices that yield them the highest benefit given their individual circumstances.

[1] Refer to the reading list on page 11 and other footnotes in this Annex for more information about behavioural economics.

2. Framing effects

Consumer decisions are influenced by how information is presented, or framed, in contracts, advertising and sales pitches. How default options are defined and presented (consumers may endow the default option with positive attributes that it may not have), and whether a choice is presented as a loss or gain, or as a low-risk or high-risk, can radically influence the decision a consumer makes.

IMPLICATIONS FOR POLICY ANALYSTS

Analysts who have reason to believe that policy initiatives will fall short of their intended objectives due to activation of the above behavioural biases may wish to pay particular attention to how information interventions are designed and how choices are framed, and defaults set, when the policy change is rolled out to the public.

The excerpt below from the OECD's *Consumer Policy Toolkit* gives examples where insights from behavioural work can help governments implement more effective policies.

Information interventions

One type of policy intervention is to provide consumers with more information about a product or service, either directly or by mandating that sellers disclose information. In order to be effective, these types of interventions must be thought through carefully. For reasons that can be attributed either to traditional models of costly information search and processing or to behavioural models, more information is not always better for consumers. Additional information may distract consumers from more important factors, and it may overwhelm consumers and cause them to make decisions with less reflection rather than more. For example, in the United States, recently developed food-nutrition labels actually provide less information than previous labels, as a way of encouraging consumers to focus on the most important contents of food.[2] In the financial area, regulation requires United States credit card companies to present key information to consumers in a table, in prescribed type sizes.[3] Many countries have adopted very short, and often graphic, health warnings for cigarettes.

[2] USFTC (2008). *Marketing Food to Children and Adolescents.* July, www.ftc.gov/os/2008/07/P064504foodmktingreport.pdf.

[3] USFRB (United States Federal Reserve Board) (2000). *Federal Reserve System: 12 CFR Part 226 (Regulation Z; Docket No. R-1070), Truth in Lending – Final Rule,* September 27, www.federalreserve.gov/boarddocs/press/boardacts/2000/20000928/attachment.pdf.

Default setting and framing

Two clear examples of the importance of default setting in the context of consumer decision making are the adoption of "no-fault" automobile insurance and the sale of reserved seats on trains. In the 1990s, two American states, New Jersey and Pennsylvania, adopted new automobile insurance regulations that gave drivers the option of purchasing lower-cost insurance that limited their rights to sue in the case of an accident ("no-fault" insurance). In New Jersey, the lower-cost, "no-fault," policy was the default, while in Pennsylvania the higher-cost option was the default. Some 70% of Pennsylvania drivers purchased the higher-cost policies, versus only 21% of New Jersey drivers.[4] Even more dramatically, a national railway in Europe found that the share of online reservations that included a reserved seat rose by five-fold when the default was changed from "no reserved seat" to the more expensive "reserved seat".[5] Finally, recent research on retirement savings in four countries shows how defaults influence retirement savings outcomes at all stages of the savings lifecycle, including savings plan participation, savings rates, asset allocation, and post-retirement savings distributions.[6]

In response to concerns about the role of defaults, the European Parliament and the Council have proposed a Directive on consumer rights which includes a clause limiting the use of default options in consumer contracts.[7] Specifically, sellers would be required to obtain express consent from consumers for any payment that is in addition to the payment for the main contractual obligation, and could not rely on default options that require buyers to reject those options to avoid payment.

As discussed above, consumers sometimes "fail to choose" when presented with a large number of possible choices. This will leave them with the default option or status quo. It should be noted that, in most cases, private sellers want to avoid this situation, as consumers who fail to choose are consumers who fail to buy. For government policy makers, however, this means that if a programme's goal is for consumers to make their own choices, the choices must be presented in a way that is manageable, both in terms of the number of choices and the way information is presented.

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4 Johnson, E. J., Hershey, J., Meszaros, J. & Kunreuther, H., A. (1993). Framing, Probability Distortions and Insurance Decisions. *Journal of Risk and Uncertainty*, 7, 35-53.

5 Goldstein, D. G., Johnson, E.I., Herrmann, A. and Heitmann, M. (2008). *Nudge Your Customers Toward Better Choices*. Harvard Business Review, 86(12), 99-105.

6 Beshears, J., Choi, J.J., Laibson, D., and Madrian, B.C. (2006). *The Importance of Default Options for Retirement Savings Outcomes: Evidence from the United States,* National Bureau of Economic Research, Working Paper 12009, January, www.nber.org/papers/w12009.

7 European Commission (2008). *Proposal for a Directive of the European Parliament and the Council on Consumer Rights.* COM(2008) 614/3, October 8, www.ec.europa.eu/consumers/rights/docs/Directive_final_EN.pdf.

FOR FURTHER READING

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APPENDIX B:
Canadian consumer organizations

Consider consulting the *Consumer Policy Research Database* www.ic.gc.ca/consumer/researchdatabase, a searchable collection of Canadian research references on consumer-related topics for examples of research studies undertaken by the Canadian consumer organizations listed below.

For assistance in finding a Canadian consumer organization that may meet your needs, contact the Office of Consumer Affairs at: consumer.information@ic.gc.ca.

UMBRELLA ORGANIZATIONS

National

Canadian Consumer Initiative (CCI)
A coalition of six consumer organizations: the Alberta Council on Aging Services, the Automobile Protection Association, the Consumers Council of Canada, Option consommateurs, the Public Interest Advocacy Centre and l'Union des consommateurs.

Tel: (613) 565-9449

Regional

Coalition des associations de consommateurs du Québec (CACQ)
CACQ is an organization which represents a cluster of more than 20 consumer associations in Quebec.

Tel: (514) 362-8623
Website: www.cacq.ca
Email: info@cacq.ca

Union des consommateurs (UC)
UC is an individual organization which represents 10 member organizations (Associations coopératives d'économie familiale - ACEFs) as well as the Association des consommateurs pour la qualité dans la construction (ACQC) in Quebec.

Tel: (514) 521-6820
Website: www.consommateur.qc.ca/union-des-consommateurs/
Email: union@consommateur.qc.ca

INDIVIDUAL ORGANIZATIONS

Automobile Protection Association (APA)
Tel: (514) 272-5555
Website: www.apa.ca
Email: apamontreal@apa.ca

Consumers' Association of Canada
Tel: (613) 238-2533
Website: www.consumer.ca
Email: info@consumer.ca

Consumers' Association of Canada - Alberta
Tel: (780) 426-3270
Webiste: www.albertaconsumers.org
Email: contact@albertaconsumers.org

Consumers' Association of Canada - Manitoba
Tel: (204) 452-2572
Webiste: www.consumermanitoba.ca
Email : info@consumermanitoba.ca

Consumers Council of Canada (CCC)
Tel: (416) 483-2696
Website: www.consumerscouncil.com
Email: info@consumerscouncil.com

Option consommateurs (OC)
Tel: (514) 598-7288
Website: www.option-consommateurs.org
Email: info@option-consommateurs.org

Public Interest Advocacy Centre (PIAC)
Tel: (613) 562-4002
Website: www.piac.ca
Email: piac@piac.ca