pattern. This leads to the hypothesis:

> H_7: families with higher medical debt will be more likely to successfully complete the program.

Two non-financial variables were included in the analysis, with the following hopotheses:

> H_8: families with more dependents will be less likely to successfully complete the program,

since more dependents place greater strain on the family income.

> H_9: stage of the family life cycle is expected to be a significant discriminator between the successful completions and the dropouts.

The total sample was segmented according to three different classifications: (1) income level, (2) number of dependents and (3) stage of the family life cycle. These were chosen as logical elements which bear upon both a family's consumption and its ability to deal with financial problems. In turn, this provides another hypothesis:

> H_{10}: variables with discriminate in one classification will not necessarily discriminate in another.

Results

The results from the entire sample are summarized in Tables 2 and 3.

TABLE 2

Summary of Critical Values: Entire Sample

Sample Size		Eigenvalue	Canonical Correlation	Significance Level	Prediction
Success	Dropout				
55	237	.04488	.207	.027	61%

Source: Data from the Consumer Credit Counseling Service of Greater Knoxville, Inc.

TABLE 3

Significant Variables: Entire Sample

Significant Variables*	Mean Values	
	Success	Dropout
1. Total debt: income 2	38.1%	46.1%
2. Medical debt: income 1	20.9%	15.0%
3. Monthly debt 2: monthly debt 1	64.7%	66.0%
4. Car payment: monthly income 1	4.4%	3.8%
5. Living expense: monthly income 1	40.5%	42.1%

*Income 1 refers to unadjusted net income. Income 2 refers to adjusted income. Debt 1 refers to debt before entering the CCCS program. Debt 2 refers to the debt payment scheduled after entering the program.

Source: Data from the Consumer Credit Counseling Service of Greater Knoxville, Inc.

Five variables were identified as discriminating between the two groups, but explanatory power and significance levels are poor. Discriminant analysis says simply that a particular variable discriminates between the two groups. The technique does not note how or why the variable discriminates. The how can be answered by referring to the mean values in Table 3. The why must be answered by the theoretical basis for the hypotheses.

Three of the five variables are aggregates--total debt to adjusted income, monthly debt in the program to monthly debt before the program and living expense to unadjusted monthly income. Referring to the table of mean values shows that hypotheses H_2 and H_3 are supported, in that successes had a lower debt:income ratio and a greater reduction in monthly debt payments. However, H_4 is not supported by the mean values; the successful completions had lower living expense allotments. This result may reflect the relation of the client's living expense while in the program to living expense before the program. However, data in this case were incomplete. Both higher car payments and higher medical bills showed a significant association with successful completions, supporting hypotheses H_6 and H_7. The successful completions had a higher medical debt and higher car payments, but a lower debt: income ratio, pointing to medical bills as the major component of their debt. The unplanned medical debt, therefore emerges as a likely source of the families' financial problem.

When the discriminant function was applied to all the cases in the sample, independent of their actual case disposition, 61 per cent of the cases were classified correctly. As the eigenvalue suggests, however, the five variables explain only a small part of the actual variation. Canonical correlation is similarly low; the significance level is .027. Thus, relationships are weak, suggesting that while certain key relationships may have been identified, other effects still predominate.

The second step in the analysis was then to segment the sample according to income level, number of dependents and stage of the family life cycle. The discriminating power of the analysis did not improve when the sample was segmented by income. Segmenting according to family life cycle did improve results, but the changes were minimal. However, when the sample was segmented according to number of dependents, the results improved significantly.

Dependents were categorized into five groups: cases with zero dependents, one dependent, two dependents, three dependents and more than three dependents. The results are summarized in Table 4.

TABLE 4

Summary of Critical Values: Sample Segmented by Number of Dependents

Number of dependents	Sample Size S	Sample Size D	Eigen-value	Cannonical Correlation	Significance Level	Prediction
0	14	39	.086	.282	.0410	68%
1	5	45	.496	.576	.0120	88%
2	12	58	.207	.414	.0580	69%
3	12	46	.690	.639	.0003	64%
3	12	49	.162	.373	.210	67%

Source: Data from the Consumer Credit Counseling Service of Greater Knoxville, Inc.

While segmentation improves results, the pattern is uneven. The variables which best discriminate do change with changing number of dependents, supporting hypothesis H_{10}, that variables which discriminate in one classification will not necessarily discriminate in another. Variations also exist in the reliability of the different discriminant functions.

Eigenvalues range from .69 in the three-dependent case (indicating that the function explains most of the variation), to only .086 in the case of no dependents. The three-dependent case also has the lowest significance level, but prediction was best in the case of one dependent, where 88 per cent of the cases were correctly classified by the function.

On the basis of the original significance level of .05, the functions in the two-dependent and greater-than-three dependent cases would be rejected. The others may be accepted as providing significant discriminating power between the two groups. While reliability does not vary systematically with number of dependents, the results still indicate that there is a relationship between number of dependents and success in the program. Furthermore, the results support the following conclusions.

In all but the zero dependent group, medical debt (expressed as a per cent of income, adjusted income or total debt) proved a significant discriminator. This supports the hypothesis that those with higher medical debt will be more likely to succeed in getting out of debt. Debt:income ratio and monthly debt 2:monthly debt 1 ratio were significant for the entire sample, but were significant in only two of the runs after segmentation by number of dependents. Car payment was significant for the entire sample and was also significant in three of the dependent group runs. The mean values of these variables support H_2, H_3 and H_6.

Some inconsistencies appear with regards to utility payments. In the run with one dependent and the case with two dependents, higher utility payments are associated with successful completion; however, in the case with more than three dependents, the converse is true making the results difficult to interpret. Since utilities are a relatively small percentage of the budget, it may be that they are a proxy for other elements. However, the sample covers a period when utility costs were rising sharply and therefore could have been causing problems. Ability to handle utility costs under these circumstances may reflect overall ability to cope with budgetary problems.

The significance level is worse (.210) for the case of more than three dependents. This suggests that as family size increases, more elements enter into the financial process making the process more complex with more variables to control for.

Conclusions

The statistical analysis answers the question: can the variables discriminate between the two groups? But in order to answer the question: why do the variables discriminate? a theoretical formulation is needed. While the first question represents a lower level of sophistication, it may nevertheless be important. A counselor, for example, could use the information in identifying families likely to have trouble getting out of debt. Even though there is not full explanation, the information can be useful in actually helping families.

Information on the number of dependents illustrates the point. While the relationship is not clear, the evidence supports the idea that there is some sort of relationship. Therefore, counselors should pay particular attention to the role of dependents in the family's pattern of consumption. Similarly, the role of car payments deserves attention, especially since automobiles are tied into both employment patterns (needing the car for work) and life style.

Extending this reasoning, the variables which were identified as significant emerge as logical topics for further research. Additional study should refine and expand the pattern of relationships. The role of utility costs is particularly important in this regard, given the increasing concern with energy and the probable impact of rising costs on families. Medical costs provide the most conclusive evidence. The behavioral implications of the hypothesis suggest that in such cases the established consumption patterns are sound and play a role in the family's getting out of debt. This finding deserves attention, particularly since its ramifications apply to broader policy areas such as national health insurance.

Having established that key aspects of consumption patterns discriminate between those who get out of debt and those who do not, the analysis indicates that further research should indeed be fruitful. Objective financial variables provide a basis for discrimination and indicate that the process is not random. At the same time, the discriminating power of these variables is limited and many questions remain unanswered. Personality characteristics were not analyzed here, but should provide additional information on how families cope with financial difficulty. Time series data would also be helpful in developing a more comprehensive analysis. Considering the cost of financial difficulty to the families involved and the public at large, more comprehensive efforts are clearly warranted.

FOOTNOTES

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10. Gary Hendricks; Kenwood C. Youmans and Janet Keller, Consumer Durables and Installment Debt: A Study of American Households, (University of Michigan: Institute for Social Research, 1973)

11. Mary E. Ryan and Scott E. Maynes, op. cit., p. 102.

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DEVELOPMENT AND VALIDATION OF A SIMULATED MARKET TO TEST CHILDREN FOR SELECTED CONSUMER SKILLS

Ms. Josephine Turner*

What skills are needed by consumers in order to function in the marketplace of the twentieth century? Can these skills be learned? If so, how might they be learned. This study investigated use of selected consumer skills by children of two ages. In order to do this it was essential to develop a measurement instrument. A simulated market was developed and used to determine each participating child's level of consumer competence.

Education aimed at increasing production skills has been a strong force in our society, while education aimed at increasing consumer skills has been minimal. Elizabeth Hoyt in the late twenties decried an educational system that fostered the development of production skills while ignoring the development of consumption skills. She proclaimed that consumer skills did not automatically come with the pay check, that they had to be learned.[1] While various consumer textbooks and guidelines have identified a variety of consumer skills needed to perform satisfactorily in a market economy, there have been few attempts to actually measure the use of consumer skills.

Among skills the consumer needs to know are: how to obtain and use information, how to pay for purchases, how to save money, how to compare packages to find which contains the most product, how to find unit price, and when to postpone present consumption. A need to change the status quo is being recognized by professional and educational groups. For example, five research goals identified by home economics administrators as research needs of this decade included research aimed toward improvement of consumer competencies and family resource use. Two specific goals were: (a) knowledge contributing to consumer's capacity to discriminate among alternatives in choice of good and (b) assessment of use of consumer information in choice making and use of goods.[2]

A consumer's capacity to discriminate among alternatives has been impaired by the increasing variety of goods offered on the market and by the pressures exerted on choice making by the mass media. While consumers make deliberate and subconscious choices daily that affect their level of living and in turn the quality of their present and future lives, their ability to assess and use information to guide these choices is often low. More information on buying skills and what

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influences their development is needed to enable educators and parents to help children improve their choice-making and buying abilities.

The purpose of this study was to investigate the use of consumer skills of children at two ages. As existing instruments measured only levels of cognitive development and not levels of buying skills, it was necessary to develop and validate instruments to measure the child's use of buying skills, and this became the primary purpose of the research.

The instruments were designed to show whether there were any relationships between the child's use of buying skills and (a) age, (b) sex, (c) occupation of head of household, or (d) money experiences and home responsibilities of the child. They were also designed to show whether market selections made by the child were related to the following purchasing procedures employed by the child participant: (a) number of alternatives examined in a market, (b) time spent in examining alternatives, (c) attempts to purchase in excess of purchasing power, and (d) examination or non-examination of a best buy.

Research Design

This study employed two different research tools: (a) two simulated markets with accompanying check sheets and (b) a parent's interview schedule. The simulated markets were developed to measure the use of selected consumer skills at three progressive levels of difficulty. Failure at a level terminated the child's participation in the testing procedure. The first level in the simulated market was developed to measure the child's ability to get a best buy. A best buy was considered to be three items as opposed to two items for the same amount of money. Level two tested the child's ability to compare quantity in different sizes and shapes of packages, and the final level tested the child's ability to compare price and quantity. The simulated markets were pretested with approximately 100 children of various ages to finalize the exact structure and merchandise to be used. The parent interview schedule, developed to record demographic characteristics of the child, opportunities provided the child by the family to have experiences using money and opportunities to share in family responsibilities, was tested at the same time. Concurrent consultation with experts in test and measurements, child development, and consumer economics occurred during development of the research tools.

Development & Validation of the Simulated Markets

A review of pertinent consumer education textbooks and guidelines suggested that among the consumer competencies a child should have are to: (a) see connections between work, income, and consumption; (b) evaluate alternatives in the market; (c) use money to purchase a good; (d) determine whether one has enough money to buy a desired item (this involves both the pricing system and coin recognition); (e) understand that one must sometimes forego present consumption and save in order to obtain a desired goal; and (f) find and use information that can help the consumer make wise selections (information to make comparisons of weight and unit price).

The following criteria were used as a guide for developing the instruments:

1. Test should be limited to a maximum of 15 minutes. It was felt that in a longer test the child was more likely to become bored and not be as careful in selections.

2. Test should reflect the real world of the child consumer, and not merely measure cognitive learning. It is apparent from the data regarding personal and family financial crises that cognitive abilities alone are not the sole criteria for consumer competencies. The literature clearly reflects that financial failures are prevalent among those who have received some classroom instruction in consumer education.[3,4]

3. Test should be relatively easy to administer to facilitate its use by different investigators.

4. Children should be tested individually and be in the home setting at the time of testing.

5. Test should measure the child's willingness and ability to: (a) determine and select a best buy; (b) work to increase purchasing power; (c) save money in order to increase purchase capacity; (d) select the package containing the greater quantity of product; and (e) compute and compare unit prices.

Description of Simulated Market

Two simulated markets were developed, one as a test and one as a retest, to measure the use of selected consumer skills at three levels of difficulty. Level one measured ability to get a best buy. Each child began with this level of the test. The child was given one piece of token money and an opportunity to earn a second piece of money. The child could make a purchase before he/she earned additional money and a purchase after earning the additional money; or the child could save the first money and add to the earned money before making a purchase. Only if the child saved money could he/she obtain the best buy. The best buy was identified for the purposes of this study as selecting one of the three available purchase selections that contained three items from the seven possible purchase selections.

Level two measured the child's ability to compare quantity in different sizes and shapes of packages. At level two the child was shown two packages containing the same product. One package contained many individually wrapped pieces and the other package contained one large size of the same product. The child was requested to tell the interviewer which package contained more of the product and how he/she determined the correct answer.

Level three measured ability to compare price and quantity. At this level of the test the child was shown three different sizes and shapes of packages containing the same or the same type product. The child was requested to tell the interviewer which package would give the interviewer the most product for the money and how he/she was able to determine this.

Validation of Simulated Market

Validity, the most important characteristic of any measuring instrument, is the degree to which a test measures the variable or variables it was designed to measure. Validity was measured by relevancy and reliability.

Relevancy. Ordinarily to determine this type of validity a group of specialists examines the various items composing the test instrument to see if they meet the predetermined objectives. A panel of 16 home management faculty and graduate students at Purdue University was requested to review the instrument and to determine on a one to five point scale if the instrument measured the child's use of the selected consumer buying skills. A rating of one indicated complete agreement, and a rating of five indicated complete disagreement. On level one of the test, 63 per cent of the panel were in complete agreement that the simulated market measured the child's ability to (a) determine and select a best buy and (b) work and save in order to increase purchasing power. Eighty-one per cent of the experts were in complete agreement that level two measured the child's ability to determine which package had more of the given product. There was 75 per cent complete agreement among the panel that level three measured the child's ability to compute and compare unit prices.

Reliability. One method of determining reliability is equivalence. Two forms of a simulated market were used, one as a test and one as a retest, with approximate time lapse of 15 minutes between them. Therefore, the equivalent method was used to determine test reliability. Using the Spearman Correlation Coefficient, a correlation between levels achieved by participants on test and retest was significant at the .003 level. The coefficient of correlation was $r_s = .3838$, a somewhat lower correlation than desired.

In essence, the simulated market met the developmental criteria:

1. The test required a maximum of 12 minutes to administer to the child.

2. Parent participants were in agreement that the test reflected the real world of the child consumer. The child usually was familiar with all of the items in the simulated markets. He/she had definite likes and dislikes of the various items and generally told the research which of the items were present in the home at that time.

3. The test was relatively easy to administer. Four researchers had experience administering it without difficulty.

4. The test was suited to individual testing in the home setting. One or both parents were interested in it and in seeing how well their child played the game. Upon completion of the test, some parents used the occasion to teach the child how to compare alternatives.

5. The test measured the child's ability to use the selected consumer skills: (a) determining and selecting a best buy, (b) working to increase purchasing power, (c) saving to increase purchasing power, (d) choosing the food package that had the most weight, and (e) computing and comparing unit prices.

Sample

The sample consisted of 62 children. Thirty childen, age four, attended four randomly selected licensed daycare programs in Tippecanoe County, Indiana. Thirty-two children attended one of eight randomly selected fourth grade classrooms, four from the West Lafayette School Corporation and four from the Tippecanoe County School Corporation. One parent or adult respondent was interviewed for each child participant. The children were equally divided in regards to sex, 31 male and 31 females.

Administration of Instruments

Data were obtained by means of personal home interviews. Child responses were obtained by playing two buying games using the simulated markets. Parental responses were elicited by interviews with responses recorded on a schedule developed for that purpose. The interview procedure was the same for all subjects. The researcher played a buying game with the child, interviewed the parent, and, lastly, played a second buying game with the child. The time lapse between test (game one) and retest (game two) for the child was approximately 15 minutes.

Analysis of Data

The following procedures were used in analyzing data: frequency distributions, coefficient of reliability, and chi-square test of independence. The rejection level for null hypotheses was set at .05. The following null hypotheses were tested:

1. The child's performance on the test and retest will be independent of demographic characteristics: (a) age, (b) sex, and (c) occupation of the head of the household.

2. The child's performance on the test and retest will be independent of money experiences and responsibilities of the child as reported by an adult respondent.

3. The child's performance on the test and retest will be independent of the child's buying procedure: (a) decision time, (b) number of alternatives examined, (c) attempts to buy in excess of purchasing power, and (d) whether or not the child examined a best buy.

Findings

Demographic Characteristics

The null hypothesis that the child's performance on the test and retest would be independent of the child's age was rejected. Older children did perform better on both the test and retest than did younger children. In the test only 28 per cent of the fourth grade children failed to complete level one of the test, while 36.7 per cent of the four-year-old children failed to complete level one. In the retest the distinction was even greater: 81.2 per cent of the fourth graders and only 30 per cent of the four-year-old children completed level one.

Twenty-eight per cent of the fourth graders completed level two in the test and 40.6 per cent completed this level in the retest. No four-year-old completed level two in the test or the retest.

Level three of the test was completed by 9.4 per cent of the fourth graders. On the retest 15.6 per cent completed this level. No four-year-old was permitted to try this level of the test as none successfully completed level two.

The null hypothesis that the child's performance on the test and retest would be independent of the child's sex could not be rejected. There was, however, a tendency for males to surpass females on both the test and retest. This was an unexpected trend since traditionally shopping has been identified as a female function.[3] McNeal found that although males were permitted to shop independently earlier than females, by age nine the females were surpassing the males in interest and experience in shopping.[5] It is possible that in this sample the females are latent in achieving skills equivalent to their male peers rather than a role reversal.

The null hypothesis that the child's performance on the test and retest would be independent of the occupation of the head of the household was not rejected. There was no evidence in this study to indicate that children reared in homes where one or both parents were classified as professional had any edge on other children in the development of these selected consumer skills.

Money Experience and Home Responsibilities

The null hypothesis that the child's performance on the test and retest would be independent of money experiences and responsibilities of the child as reported by the adult respondent was rejected. An unweighted index of opportunities provided the child by the family to use money and to share in family responsibilities was computed for each subject from responses given by the adult respondent. (See Table 1.) A score of one was assigned for a positive response to item 10 reported as frequently as twice weekly and for all other items reported as frequently as twice monthly. One point was given for each category in which the child participated in the decision process. For example, if the child helped make decisions regarding purchases of cereal and fruit one point was assigned for participation in food decisions. One point was assigned for each regular home responsibility of the subject. The total points for a child comprised his/her index of opportunities to use money and share in family responsibilities.

For the purpose of testing, these scores were grouped into three classifications: low scores (0 to 7), medium scores (8 to 11) and high scores (12 to 16). The null hypothesis was rejected at the .05 level of significance. The level achieved by children on the test and retest was dependent upon the opportunities provided the child by the family to use money and share in family responsibilities. The more opportunities available to the child to participate in the consumer decision making process and the more home responsibilities the child assumed, the higher score the subject earned on the test and retest. (See Table 2.) When each score item was separately examined, only one, shopping alone, was consistently within the rejection range. That is, children who were permitted to shop alone earned higher scores on the buying games than children who were not allowed this privilege.

Table 1

Unweighted Scoring Procedure for Index of Opportunities Provided the Child by the Family to Use Money and Share Family Responsibilities

Item	Response*	Points
1	Usually has money to spend	1
2	Regular amount of money	1
3	Allowance as source of money	1
4	Shops with parents	1
5	Shops alone	1
6	Shops with siblings or peers	1
7	Helps family make decisions about purchases	1
8	Kinds of decisions	(0 - 5)**
9	Pays for selected items	1
10	Decided clothing to wear, twice weekly	1
11	Family responsibilities	(0 - 5)**
12	Savings with goal in mind	1
13	Categories of expenditures	(0 - 3)**

*One point was given for each item reported as frequently as twice monthly, except for item 10.
**One point was given for each different category mentioned in the interview.

Table 2

Highest Level Achieved in Test and Retest by Opportunities Provided the Child by the Family to Use Money and Share Family Responsibilities

	Test						Retest					
	Low		Medium		High		Low		Medium		High	
Level	N	Cum %	N	Cum %	N	Cum %	N	Cum %	N	Cum %	N	Cum %
Three	(0)	0.0	(0)	0.0	(3)	20.0	(0)	0.0	(3)	12.5	(2)	13.3
Two	(1)	4.3	(3)	12.5	(2)	23.3	(0)	0.0	(2)	20.8	(6)	43.3
One	(12)	56.5	(13)	66.7	(8)	76.6	(9)	39.1	(7)	49.2	(6)	80.3
None	(10)	100.0	(8)	100.0	(2)	100.0	(14)	100.0	(12)	100.0	(1)	100.0
	23		24		15		23		24		15	

X^2 = 13.060, 6 d.f., > X^2 = 12.5916 at .05 level of significance for test.

X^2 = 21.7899, 6 d.f., > X^2 = 18.5476 at .005 level of significance for retest.

Buying Procedure

The null hypothesis that the child's performance on the test and retest would be independent of the child's buying procedures was tested. Four aspects of the child's buying behavior were tested: (a) number of alternatives examined; (b) time spent in examination of alternatives and decision making: (c) attempts to purchase an item in excess of the available purchasing power; and (d) examination or non-examination of best buy.

The null hypothesis was rejected at the .05 level for only one of the above aspects of buying behavior tested, namely, time spent in examination of alternatives and decision making. Children who required between 101 and 200 seconds to examine the alternatives and select a purchase achieved a higher level on both the test and retest than children who required more or less time. The level achieved on the test and retest was indicative of an optimal amount of search prior to decision making. Either too little or too much time spent in search reduced the chances that the child would obtain a best buy in level one of the test. These findings might be accounted for by the fact that children who tended to be more sophisticated in the search procedures used a method of examining alternatives that required less time than was spent by children who examined alternatives at random, that is, without a method.

Conclusions and Implications

A simulated market was developed that effectively measured the child's use of selected consumer skills: (a) ability to determine and select a best buy; (b) willingness to work and to save in order to increase purchasing power; (c) ability to determine which package has more; and (d) ability to compute and compare unit price. The effectiveness of the test is demonstrated by the correlation between the test and the retest. The simulated market is unique as it marks one of the first times a behavioral measurement of consumer competence has been developed and shows that consumer skills related to buying behavior can be measured. It can serve as a valuable complement to cognitive testing and be an enjoyable experience for the child.

The research findings attest that consumer competence as measured by the buying behavior of children varies directly with their age, home responsibilities and money experiences, and somewhat indirectly with the time spent in decision making. Children who spent more than 200 seconds and children who spent less than 100 seconds in deciding upon an alternative(s) made poorer decisions than those who spent between 101 and 200 seconds.

The simulated market could possibly be used as a means of evaluation and consumer education in both home and school. With modifications or adaptations, the market game could be used to evaluate the child's competencies in a variety of other consumer skills, such as, value identification, quality perception, and evaluation of information.

FOOTNOTES

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CONSUMER PROTECTION AGENCY: AN ADVOCATE VIEW

Ms. Esther Peterson*

There is an increasing interest in the consumer field as a profession. The time is coming when we will consider consumerism in the corporate picture as well as the legislature. We should encourage support for the Consumer Protection Agency. There is a need for accuracy in promoting public understanding of this agency. The purpose of the bill is to correct the imbalance that is in the marketplace today, but this purpose is lost in the deliberate misrepresentations or exaggerations given by some businesses.

There is an increasing interest in the consumer field as a profession. The time is coming when we will consider consumerism in the corporate picture as well as the legislative. But presently, my assignment is to assist on a limited basis to encourage support for the Consumer Protection Agency.

There is a need for accuracy in promoting public understanding of this agency. The purpose of the bill is to correct the imbalance that is in the marketplace today, but this purpose is lost in the deliberate misrepresentations or exaggerations given by some businesses. The testimony of the Chamber of Commerce shows its unwillingness to admit that consumers have the same rights in Congress as the large companies.

Consumerists are so out-numbered and so off-balance that there is no argument for the imbalance of this little agency. The Chamber will not accept the consumer's right to be heard by regulatory technicians, and this is causing it to deliberately misstate the case. The small consumer agency proposed by the President is an attempt to equalize what we have known for a long time about an imbalance in our system. In testimony before Congress, Chamber representatives misstate the purposes, content, and effects of the proposed legislation to create a voice for consumers.

Major modifications and safeguards in the bill have been accepted over a period of eight years. These modifications have helped the business cause. Despite this, the Chamber's opposition is still very evident.

Many business people support the bill. One indicated:

> We believe that having a separate consumer agency with the authority to represent consumers interest in proceedings of other agencies will improve the prospect of such interest being consistently and fully considered. This will give consumers additional grounds for confidence in the fairness and

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soundness of our government's procedures and decisions which affect the pocketbook of all of us.

Many other businessmen agreed. The point is that at least we recognize each other's rights. This is not an anti-business bill--it is an equalizing bill which is terribly important.

The purpose of the bill is to assure that the interests of consumers is adequately represented and protected within the federal government because such representation is essential to the fair and efficient function of a free marketplace. The goal is to protect and promote the interests of the people of the United States as consumers of available goods and services. This agency bill is the cornerstone of future bills to promote the goal.

NATIONAL TELECOMMUNICATION

PUBLIC POLICY ISSUES

Dr. Lee Richardson

The telecommunications industry is faced with radical change. Technology is raising the possibility that competition can enter the scene by passing the utility restrictions that have allowed telephone to function as a monopoly. Telephone is an industry with one company holding 80 per cent of the market so that change must be viewed mostly as impact on that one firm, AT&T. Issues include political and economic ones for which we are unprepared in large part. There is no precedent nor can we conduct experiments that are easily reversed.

Pressures that may dramatically changethe telecommunications industry have been mounting recently. Certain elements of competition have been introduced into the telecommunication system by the Federal Communications Commission by regulation rather than new laws. Acting under authority of some thirty years plus, the FCC has been introducing a series of changes that it thinks is appropriate, basically adding limited amounts of competition into this industry where it did not exist. An event that occurred in 1974 but still is in litigation is the Department of Justice suit to eliminate the monopoly of the one company that dominates roughly 80 per cent of this industry, American Telephone and Telegraph. If successful, it will radically change the structure of the industry. Also a year ago the Consumer Communications Reform Act of 1976 was introduced by the telephone companies themselves. This Act would essentially restate the public utility concept, but also have some important effects upon the trends the FCC has been initiating and upon the Department of Justice effort to break up AT&T, both vertically and horizontally. While these events have suddenly come upon us forcing us to think about the issues, rapid technological advances promise great improvement in communications if technology is appropriately nurtured and directed through regulation and organization of the industry.

If it is a government-approved monopoly, one assumes that a public utility is to be directed by the government that licenses or franchises it. That is one element of government direction. The second element is that it is done in areas where the service or item provided is considered by society to be indispensable. All those who can reasonably be expected to pay for it and can reasonably pay for it are generally assured of some reasonable amount of that service. Those who want it can get it with certain modifications. This leaves the government in charge, with the basic problem of offsetting profits and directing the service that will be provided at what prices, on what burdens, to whom,

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for this kind of a service. And we have not always had this kind of a concept. This is a rather unique form of running institutions that provide products and services.

1907 was the beginning of the public service commission movement, and the intra-state telephone system. It was not until 1910 when the ICC was first given the job of regulating the industry, that federal regulation of inter-state telephone service really got underway. So at the national and state level a lot of things happened in the evolution of the industry without really any oversight of what we now all agree is basically a utility situation. Then in 1934 the Federal Communications Commission took over from ICC under a new law which is basically what we are living with today--federal regulation. In 1935, for example, the FCC praised the quality of the work done by AT&T--for its services, financial and accounting practices, in spite of the fact that the ICC really had done little regulating. The company had arrived somehow in 1935 with this interesting, mixed history of regulation. In an anti-business climate it was really a unique statement to make about an industry, particularly about a company that overwhelmingly dominated its industry.

Today, we have the national telecommunications network of phones connected to each other by local and long distance connections, switches and so forth. The Bell System alone, accounting for about 80 per cent of this, has 123 million phones connected to each other; the other 20 per cent of phones are represented by other companies. This network carried a half billion calls per day in 1976, including about 35 million long distance calls that obviously used many pieces of the network in being put together. AT&T itself is a holding company subject to the usual rules of holding companies. But though it is under the same basic laws, AT&T does not have the same kinds of problems as American Electric Power or Southern Company or Middle South Utilities.

There are some costs that people in rural areas and special situations incur, but universal service is generally present. Can you have that universal service (and perhaps subsidize it because society needs access to the telephone), and then bring in competition in other elements? This is one of the central issues the Consumers Communication Reform Act presents. Can you have a system that is partly regulated, including some subsidized services perhaps, and yet bring in competitive prices to meet the market prices at the same time in other parts of the system. If handled incorrectly, the regulated portion of the system may gain higher rates to subsidize the battles in the competitive sector. To avoid that, should we put rules on the regulated portion that prevents it from cutting prices unfairly? Should we have different rules for the free competitors that have no regulated utility duties to bind them? It sounds plausible and worth considering. What about the difference in the capital cost of the different parties in the competitive battle? AT&T has certain access to capital that is not available to other kinds of firms, large or small. Is that good or bad, or how much of a differential exists in the first place?

Another kind of political science problem is the question of size alone that many like to raise. The Bell system, with 900,000 employees in every community in the country, has clout in local, state, and national political decisions, regulatory and legislative. Its access to legal power enables it to tie up the processes of regulation and law. What about the size of the company versus separate states. Is it really South Central Bell versus Mississippi, or is it AT&T versus Mississippi? Is that balance there? Is that workable? And then what is the consumer's position, or the customer's ability to get into this mix. We need to establish a fundamental philosophy in anti-trust. Is there a size beyond which you should not go? If we think there is something wrong with that much size for political reasons, can we come up with ways of offsetting the impact of the size other than the most radical types of surgery such as divestiture or breaking up the biggest company, or as some suggest by nationalizing AT&T? It is a critical question. It may sound to an engineer or an economist like the wrong kind of question, but it is one that has to be faced.

The issue before us today is to be seen in the context of these points. Take a look at the Consumer Communications Reform Act and be thinking of the questions you want to ask and the impact of the various proposals you will hear. Does the CCRA move in the right direction? Is CCRA even a very central issue? Just how important is the CCRA in all this national public policy debate? What sort of process should we be using to decide these issues? Should we let Congress go ahead this summer and pass the law and set it in concrete, or is it a case for further study or input by various other interests? What sort of political process would you suggest? What additional questions on the pros and cons of CCRA need to be asked? I think we have two or three people here who can deliver some of the results we need.

CONSUMERS' CHOICE OR ECHO: COMPETITION OR MONOPOLY IN TELECOMMUNICATIONS

Mr. Ian Volner*

The paper analyzes the debate which is now raging before the Congress, the Federal Communications Commission and the courts whether the consumer is best served by permitting the Bell system to maintain a monopoly over the provision of all telecommunications services in the United States. Briefly tracing the history of evolving policies which have permitted competition, particularly in the provision of terminal equipment, it points out that the introduction of competition is beneficial to consumers because it creates meaningful economic choices which enable the American public to secure telephone service and equipment suitable to its needs at a favorable price.

A central debate which is now raging before the Congress, the Federal Communications Commission and the courts is the future of telecommunications policy in this country. The issue is whether the consumer is best served by allowing telephone companies to artificially maintain a monoppoly over the provision of all telecommunications service to the American public; and through its monopoly position to absolutely control the choice of products which are made available to and the prices which are paid by the consumer. The Bell system and its independent telephone company allies seek to implement this policy through legislation which has been introduced in the Congress which would have the effect of prohibiting competition in the telecommunications field. The bill is called the Consumer Communications Reform Act of 1977.

The alternative choice is to continue--and strengthen--the existing policy which permits entrepreneurs to compete with the telephone companies in the provision of certain services on the premise that competition enhances the choices available to consumers and operates to maintain lower prives. This choice is presented by the independent manufacturers, suppliers and distributors who furnish terminal equipment to telephone customers. These companies are frequently referred to as the "interconnect industry."

In order to understand the benefits which a competitive telecommunications policy has yielded, it is unavoidably necessary to review how we got here. Shortly after it was created in 1934, the FCC was required by Congress to submit a report on the state of the telecommunications industry which consisted, in those days, solely of the telephone and telegraph networks. The Commission found the existing network was already too well developed to permit the immediate introduction of unrestrained competition. However, it noted that competition would be beneficial if introduced in an orderly manner.

The first significant step toward the development of a national policy of telecommunications competition was in 1956. In that year, the

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Commission struck down a Bell system regulation which prohibited telephone consumers from attaching a plastic cup to the mouthpiece of their telephones. The Commission and the Courts both found that the Bell policy was an unwarranted interference with the telephone subscriber's right reasonably to use his telephone in ways which are privately beneficial without being publicly detrimental.

This principle, that telephone customers should not be denied the right to use their own telephone terminal equipment so long as it does not impair the network, was expanded and reaffirmed in a 1968 decision which goes by the name Carterphone. It is that decision which is primarily the foundation upon which the interconnect industry has come into being. Earlier, in 1959 the Commission introduced for the first time a policy of allowing large users to build and operate their own private microwave systems, using certain frequencies set aside by the FCC for this purpose. This determination is the basis for the specialized common carrier industry which provides private line communications for special purposes. Thus, our existing national policy of competitive telecommunications is confined to two discrete and clearly defined areas. It exists only with respect to terminal equipment--the "interconnect industry"--and with respect to private line special communications--the "SCC's".

The area in which existing policy permits competition is, in terms of the total telecommunications industry, quite small. In 1957, the total domestic telecommunications market amounted to $35.3 billion in revenues. The two areas in which competition exists--private line and telephone equipment--totalled approximately $4.2 billion, or slightly more than ten per cent of the entire market. Even if, by reason of superior products and lower prices, the interconnect and SCC companies were able to drive AT&T and its allies entirely out of the two areas in which competition is permitted, the telephone companies would nevertheless be left with an absolute monopoly in over 90 per cent of the total telecommunications field. Moreover, whatever may be thought of AT&T's products, its services and its practices, the telephone companies are and will remain a force in the terminal equipment and specialized carrier fields. In 1975 the combined revenues of the specialized common carriers and the private terminal equipment manufacturers amounted to one-half of one per cent of total telecommunications revenues. The interconnect industry represented in that year approximately five per cent of total terminal equipment sales. Unlike AT&T, we do not ask that the telephone companies be banished.

The very force and cost of the campaign which AT&T has mounted to abolish these young industries arouses suspicion. It is difficult to understand exactly what threat Bell perceives from the competition which it has experienced in these areas. The stated reason given by Bell in support of the Consumer Protection Act cannot be the real reason. Bell's campaign for the Consumer Protection Act rests upon two very simple propositions. It maintains that unless it is allowed to perpetuate and, indeed, extend its monopoly position, rates to consumers will go up and the quality of service will go down.

The claim is fallacious. The fact is, there is not proof that competition has increased telephone rates for consumers. On the contrary, the available evidence shows that competition in the terminal equipment field is beneficial to consumers because it creates meaningful economic choices, enabling a consumer to secure telephone service and equipment which suits that consumer's needs at a favorable price.

The FCC, which has historically shown great sympathy and sensitivity to the telephone company, can find no evidence that the existence of competition will increase the cost of service to the consumer. Nor has anyone else been able to find any extrinsic evidence to support Bell's contention that competition in the interconnect field means higher residential rates. It is true that residential rates have gone up substantially in some states in which Bell faces significant competition from the interconnect industry in the provision of terminal equipment. It is also true, however, that rates have gone up substantially in a number of states where Bell faces no competition whatsoever. Bell's residential rates have nothing to do with the existence or non-existence of competition.

At best, then, the claim that competition will result in increased costs to consumers is hollow. At worst, it is no more than an excuse--a cover-up--to justify anticompetitive policies, designed to perpetuate Bell's absolute control over the prices it charges and the service it provides to all consumers. To the extent that Bell faces competition from the specialized common carriers and the interconnect industry, the competition thus far has been most intense in the provision of services and products to business users. Bell claims that the potential loss of business in the business sector deprives it of its greatest "profit." It contends, in other words, that it has been overcharging the business user in order to keep rates for the residential consumer lower.

Bell's claim has a certain Robin Hood-like appeal to it: take from the rich in order to protect the poor. In fact, the situation appears to be just the other way around. Bell is playing Robin Hood in reverse.

The evidence shows that it is <u>overcharging</u> the residential consumer in order to <u>underprice</u> services it provides to business users. The motive behind this is equally obvious. By underpricing its competitors, including the interconnect industry, Bell can maintain its monopoly control over the entire telecommunications market. This enables Bell and its allies to continue to charge <u>all</u> consumers--business and residential--largely as it pleases. At the same time, it will enable Bell to eliminate the other benefits--such as increased employment and improved balance of trade--which competition offers.

If you still believe that the existence of competition in the terminal equipment field is calculated to produce increased consumer rates, ask yourself these types of questions:

*Why should a consumer be forced to pay $1,200 for a $24 telephone instrument over 20 years of paying his phone bill when he can purchase the unit outright at its true economic cost?

*Why should a consumer be forced to pay $60 or more in some places to move his telephone from one residence to another when, with proper connections, he can move the phone himself at no cost?

*Why should a consumer be denied a choice of type of telephone instrument he wants to have? Increasingly, there is a need for highly sophisticated communications facilities to deal with the very way in which we live; and increasingly, with the development of new concepts--such as electronic banking, electronic bill-paying, etc.--the need for this sophisticated and effective equipment spreads to all levels of our society. Bell claims that its competitors have not provided one single new or innovative service. The very existence of the young, but vibrant, interconnect industry belies this claim. Indeed, the existence of competition has forced Bell itself to respond more effectively to new and developing consumer needs. There is copious evidence that until the late 1960's the Bell system and its independent telephone company allies responded to consumer needs with caution or ineptitude. With the advent of competition, Bell has been forced to respond to the innovations wrought by its competitors by itself providing products which better serve needs at lower costs. The situation is the classic textbook example of the principle that monopoly promotes stagnation while competition releases creativity. The ultimate beneficiary has been the consumer.

There is one other aspect of this debate as to the merits of a competitive telecommunications policy which is or at least should be of consumer concern. It is the question of employment or unemployment. Over all, employment in the Bell system has declined by about 200,000 between 1970 and the end of 1976. This has led some critics of competitive policies to imagine that there is somehow a causal connection between competition and unemployment.

The facts contradict such a conclusion. Indeed, in its chief field of competition--with the interconnect industry--the Bell system has experienced a net increase in employment. Independent telephone companies have also added more workers in these categories. It may be that these gains are entirely independent of competition from interconnect firms. Indeed, the ups and downs in Bell's employment show very little pattern at all. Certainly, however, there is absolutely no merit to the claim that the existence of a competitive telecommunications policy has increased unemployment among those who would otherwise have been employed by the telephone companies.

The existing telecommunications policy of competition in limited areas has been good for the consumer because competition makes it possible for a consumer to obtain the services he wants at the price he can afford. It forces the telephone company to work harder, more imaginatively and more economically. Two decades ago we might have said "what is good for Bell is good for the country." But, I believe that if we have learned nothing else in the last 20 years of consumerism, we have learned that the opposite is true. This is the best reason of all for maintaining and strengthening a competitive telecommunications policy.

MEETING CONSUMERS' NEEDS IN TELECOMMUNICATIONS

Mr. Theodore L. Simis*

Far-reaching technological advances, new communications needs and possibilities and apparent inconsistencies in government decisions have resulted in some confusion and uncertainty in the telecommunications industry. The present situation cannot be allowed to continue; Congress must reexamine and redefine our national telecommunications policies. Goals and guidelines established by Congress--as with the telecommunications system itself--must be socially, structurally, economically and technically sound.

The issue in telecommunications that requires our attention and that of every American family is not the narrow and frequently misrepresented question of whether competition should be allowed in telecommunications. Competition already exists in this industry. The questions that remain with respect to competition have to do with defining those telecommunications areas where competition is in the best interests of the public and with establishing whatever regulations are required to protect these interests.

In so many areas--health services, transportation, consumer products--needs are constantly changing and becoming more sophisticated and challenging. This is especially so in communications. In this vital area of our society changes have been occurring rapidly and constantly since the Second World War and there are no signs that they are about to cease or even slow down.

It is an undisputed fact that the United States has the very finest telecommunications system in the world today. To an important degree, this achievement has resulted from the establishment of clearly defined national telecommunications objectives and policies. But that is no longer entirely the case. Far-reaching technological advances, new communications needs and possibilities and apparent inconsistencies in government decisions over the past several years have combined to place the telecommunications industry in a state of some confusion and uncertainty.

At the very outset then, we must ask ourselves what communications capabilities our people will require a decade from now and in the years thereafter. The present confusion must not continue. We--that is, both the telephone industry and consumers--need a reexamination and redefinition of our national telecommunications policies by our elected representatives--the Congress of the United States. Congress has both the authority and the responsibility to set forth goals and guidelines in this area, as in others, and there can be no hope that your sophisticated future communications needs will be met unless the Congress exercises its reponsibility in this regard.

*Assistant Vice President-Staff, AT&T

The goals and guidelines established by Congress--as indeed, the telecommunications system built thereupon--must be socially, structurally, economically and technically sound.

Social

From a social viewpoint, our national telecommunications policies must derive from and adequately reflect the needs of the American people. Some 43 years ago, in the Communications Act of 1934, Congress set forth as our national telecommunications goal

> ...to make available, so far as possible, to all the people of the United States a rapid, efficient, nationwide and worldwide wire and radio communications service with adequate facilities at reasonable charges...

How well that lofty and challenging goal responded to the country's needs can be gauged by the fact that in large degree it has been accomplished and by the high quality of our telecommunications service today.

At the present time, as subcommittees in both the Senate and the House of Representatives begin efforts to forge a new statement of national telecommunications objectives, residential customers and consumer groups like your own, along with various other interest groups, should make their viewpoints known. Congress needs the broadest possible representation on the issues and the needs that must be met.

Your contribution is vital and I have been encouraged by the ongoing dialogues between business and industry--including the telephone industry--consumers both individually and as represented by organizations and a wide spectrum of other informed persons and groups. Such dialogue is necessary to assure full exploration of the social aspects of communications as well as timely and appropriate responses to society's needs.

Structural

Structurally, it is important to be cognizant of the extremely intricate and delicate nature of the telecommunications network, as well as the managerial skills and accountabilities necessary for it to function and expand. The telecommunications system is the neural network of this nation, serving--much like the nervous system in your own body--to receive and transmit messages from both within and outside the nation so that both individuals and the nation can properly function.

Underlying every form of communications between people and their information and process mechanisms is a vast and complicated network (and I am not here referring only to the telephone network) made up of switches; computers; wire, radio and lightwave paths; stores of information; and people. This unique system that we as a nation possess in both a physical and informational sense, can be utilized to perform virtually any conceivable set of activities having to do with communicating. It extends to any human activity involving the use of information--for example, the control of processing or manufacturing, electronic funds transfer, law and library retrieval systems, educational programs, defense systems, and various other needs of this nation.

It would be ironic if in an era when we are coming to recognize the need for large-scale systematic planning in some of our society's basic undertakings--transportation, the supply of energy, the delivery of health services--we should at the same time apply to the very industry that has served as the model of such planning, ground rules more appropriate to a past age. The core of the information infrastructure of this nation is a basic telecommunications network, designed and managed as one entity. It will serve to link terminals and subsystems of a variety currently beyond imagination and should be circumscribed only by the requirement that there be no undue risk to the operation of the infrastructure network as a whole.

This concept for tomorrow will require clearer and more precise definitions of the natural monopoly and competitive areas of telecommunications. New modes of regulation may be needed. Improved standards of interconnection and privacy will be required. This will not be altogether new for the telephone industry. Long ago we recognized and accepted the public interest and public service objectives as the very purpose of our industry.

Telephone customers, for their part, have long been secure in knowing that accountability for their telephone service rested squarely with the phone company. If parts of the system are now to be removed from the phone company's responsibility, accountability for the service those parts represent will necessarily pass to the customer--with all of the attendant consequences in service costs that entails. Unified management of the network and accountability for it has the further advantage of facilitating optimum long-range planning and technological innovation. The very concept of a network implies an integral whole, a unified system. In such a concept, duplications and gaps are equally unacceptable. A nerve system that does not reach to all parts of the body or which favors some parts over others is no longer performing its proper function.

Terminal equipment manufacturers and suppliers say that since their entry into telecommunications, consumers have a far wider choice of telephone equipment and that telephone companies have improved their service. To some degree, this is undoubtedly true. We must be careful, however, not to confuse product differentiation with basic system innnovation--the substantive technological changes represented, for example, by the transistor, microwave and satellite transmission, electronic switching systems and fiber optics--that keep our telecommunications network in step with society's needs. I think of this network as a living thing, constantly being revitalized and updated to make it a more suitable instrument for people to communicate with and interact with one another. This basic systemic innovation, this continual revitalization process, is made easier if the basic network is maintained and operated as a unified whole.

Economic

You have a particular interest in how telephone services are to be priced. Underlying traditional telephone price structures has been what we call cost and rate averaging. Charges for basic exchange service are the same, for example, for two customers in a given community even though one lives in an apartment building near the telephone office and the other lives in a private home on the outskirts of town. A long-distance call between two large cities costs the same as a call between two rural communities, provided the distance is the same and the calls are alike in time, duration, etc. Traditional pricing structures have served home telephone users well, without them we would not have the telecommunications system we now enjoy. They would serve as admirably in helping us meet the nation's future communications needs.

Competitive pricing standards may have a place in certain areas of telecommunications, but let us not imagine that those standards and the public interest are one. Under competition, prices for any service are necessarily driven toward their costs--a necessity in direct contrast to cost and rate averaging--and a far cry from the established principle that affordable service be furnished to every household. Our endeavor has been to provide quality service at reasonable charges to all the people of this nation.

If we are to select a new set of pricing standards for telecommunications services to replace those that have served us in the past, let us at least be aware beforehand of the implications of such a choice. Scarcity of some materials, rising energy and labor costs and inflation generally, along with other factors, have forced us to raise telephone rates across the country in recent years and to realign rate structures for different services. Customers, faced with higher costs in so many other areas at the same time, have understandably complained of higher telephone bills. Any of you who may be looking to competition to ease the burden on residential telephone customers, should know that, on the contrary, competition will likely bring a restructuring of rates and such a restructuring could easily result in even higher telephone bills for some--in particular for residential customers.

Technical

Lastly, unless our telecommunications system is technically sound, we have no system at all. The core telecommunications network, once again, is a unified, finely tuned and delicate instrument and must be carefully managed as such. It must be protected from harm by inferior, malfunctioning or improperly connected equipment. The parts that go into the system must be manufactured according to prescribed specifications, installed and maintained properly, and repaired quickly if they fail. The network requires large-scale, long-range planning that cannot be done haphazardly and piecemeal.

Having set forth these fundamental considerations, let me state some of my own convictions:

--Congress, as your voice, is the appropriate body to set national telecommunications policy.

--The basic affordability of home telephone service should continue to be a prime goal. If that is the case, a pricing structure should be established where revenues from other services will continue to help keep basic home rates low.

--Where competition is to be the rule it should be real competition, with no protective umbrellas for certain suppliers.

--Regulated monopoly should prevail in those areas where economies, efficiencies and the public interest make it preferable to competition.

--Wide consumer choices in products and services should be available. At the same time, we must maintain network integrity and undiminished service quality.

--There should be the widest exploitation of new technologies, for the benefit of all users.

In conclusion, I would like to endorse the commitment made by AT&T's Chairman, Mr. John DeButts, at the national meeting of the Conference of Consumer Organizations last December:

> ...These, then, are our accountabilities--to serve you well, to strive always to serve you better, to treat you as an individual and not a number, to charge you fairly, to listen to what you say, to heed it and, finally, to speak out whenever policies are proposed that put our abilities to serve you at risk. Perhaps at times we'll fall short of these accountabilities. Nonetheless, these are the standards that we set for ourselves, the standards by which we are ready to be judged.

CONSUMER REPRESENTATION IN SETTING SAFETY STANDARDS

Mr. Victor P. Petralia*

A main responsibility of the Consumer Product Safety Commission is the development of safety standards for products that have been shown to present serious risk of injury to the public. Between innovative legislation by Congress and enlightened policy of the Commissioners, public involvement in standard setting is a rule in CPSC. Fully one-third of any group selected to develop a Consumer Product Safety Standard are consumers. They participate in all phases of development contributing either their scientific expertise or their concerns as ultimate users of the product. CPSC urges all interested persons to get involved in the process.

In the Area of Standards Development, the Consumer Product Safety Act specifically says two things:

1. The purpose of this act is to develop uniform safety standards for consumer products...(Section 2(b)(3))

2. The Commission shall prescribe regulations ... to include requirements ... for notice and opportunity by interested persons (including representatives of consumers and consumer organizations) to participate in the development of such standards (Section 7(d)(3)(B).)

Since creation in 1973, the Consumer Product Commission has given highest priority to its policy of consumer participation in standard development and to its general policy of openness to the public.

The Commission has established and consults with its product safety advisory counsel regarding safety standards. By holding consumer feedback sessions around the country, by widely distributing our public calendar of Commission activities, and by creating the toll-free hotline the Commission has aimed to reach out to the consumer as well as provide access for reaching in by consumers to the activities by CPSC. By liberally interpreting the Freedom of Information Act, and assuring that nearly all Commission meetings are open to anyone willing to attend, the Commission has conducted the public business in the public eye.

So that the consumer's position is heard directly by the Commissioners, an organization known as the Office if Public Participation has been proposed. When created, the office's primary function will be to provide

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an organizational mechanism to fund certain public participants in Commission proceedings.

The Commission wishes to develop Federal Safety Regulations in a public forum with both consumer and industry involvement. The law prescribes that CPSC take certain steps when promulgating standards. Among them are: giving public notice, describing of the risks to be addressed, exploring existing standards in effect, and inviting qualified interested parties to develop the standard in question. The offerors can be and have been consumer groups, private laboratories, universities, government agencies, trade associations, and others.

As noted in my opening comments, the law specifically requires the opportunity for consumer participation no matter who develops the standard. The CPSC has met this spirit as well as the letter of this directive. Whenever an offer to develop a standard is extended by CPSC, strict guidelines regarding consumer involvement are stipulated.

In the Federal Register announcement (March 31, 1977) the Commission specifically states:

> It is the Commission's desire that consumers be afforded an opportunity to fully participate in the development of standards. The Commission believes that it is essential that offerors include as members of the commitee that actually drafts a recommended standard both use-oriented consumers and consumers who are technical experts in this subject matter of the standard under development.....
>
> The Commission believes that at least 1/3 of the persons directly involved in the development of the standard should be consumer.

When the proposals from the offerors are received, the section dealing with consumer involvement is critical in final selection.

The offeror process has been extended eight times: for architectural glass, matchbooks, swimming pool slides, lawnmowers, color tv receivers, public playground equipment, Christmas tree lights, and aluminum wire.

Essentially there have been three types of participation by consumers at two levels of involvement. Technical consumers are experts in the subject matter of the standard under development who have no business interest in the standard. For example, a professor of electrical engineering might be a technical consumer for the minature Christmas tree light standard. A use-oriented consumer would be a person to whom the consumer product would be sold. Anyone who has bought and used Christmas tree lights would be eligible to participate. For lack of a better term, both the technical and use-oriented people might serve as "administrative" consumers in the standard development process. The volumes of information and comments that are collected during the development process must be analyzed and tabulated. The consumer representatives contribute in this area as well.

There are two levels of involvement by consumers in the standard development process. There are consumers who attend meetings, express their thoughts and recommendations, and discuss the issues at hand. In addition, the offeror process allows for consumers to correspond with the committee developing the standard by letter. In the past, consumers who participated by attending meetings, would count on contributing approximately two days per month for approximately one year attending the meeting plus additional time at their homes studying the issues. Consumer representatives who have participated have thought the experience worthwhile. They feel that they have contributed to the standard under development. In the beginning, many were skeptical about their reception; however, they later found themselves well received and listened to by the offeror. As in all committee work, some have felt frustration in getting the job done. Others have felt overwhelmed by the technical issues presented by the offeror and would have preferred more of their own technical support.

This system is an elaborate and involved one. It has been criticized by some as not being time-efficient. Many people in CPSC as well as outside the organization have made recommendations to modify the process to make it run smoother.

There are several ways to be considered for participation. A person can apply directly to the Secretary of the Consumer Product Safety Commission to be placed on our computerized list of interested parties. Since the Commission announces the organization selected to develop a standard publicly and since the Commission requires that the organization selected publish its proceedings far and wide, an interested consumer can express his interest for participation directly to the offeror.

DEPARTMENT OF COMMERCE AND CONSUMER PROTECTION

Mr. Gene Cope*

There are a number of agencies within the Department of Commerce whose functions results in very direct and significant consumer impact. They include: National Bureau of Standards, National Marine Fisheries Service, National Fire Prevention and Control Administration and Domestic and International Business Administration. The Consumer Affairs Division role as "in-house consumer advocate" is to bring the views of the consumer into balance with those of business in policy and program decisions of the Department of Commerce.

Concern with consumer affairs is nothing new for the Department of Commerce. There are a number of agencies within Commerce whose functions result in very direct and significant consumer impact. They include:

1. National Bureau of Standards--which is active in the areas of weights and measures, product labeling, energy efficiency, and standardization;

2. National Marine Fisheries Service--which conducts on-site voluntary seafood inspection programs;

3. National Fire Prevention and Control Administration--which reviews the causes of fire, fire codes and equipment, and home safety measures, and makes recommendations to fire departments throughout the country; and

4. Domestic and International Business Administration--which is involved in trade negotiations, short supply export controls, and other commercial practices, and which administers the Department's field office program. The Office of the Ombudsman in the Domestic and International Business Administration provides information and assistance to both business and consumers.

In addition to these on-going programs, there are a number of new activities at Commerce which focus on the consumer. For example, a Consumer Affairs Council has been established to advise the Secretary on consumer matters. The Council membership consists of heads of all the units within the Department which have consumer-related functions. It is chaired by the Assistant Secretary for Administration. The Council meets monthly to analyze policies and programs throughout the Department, and to make recommendations to policy officials which will best serve the consumer's interest. It frequently confers with consumer leaders to keep abreast of their concerns and obtain their input on issues.

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Second, the Secretary has directed the consumer representatives be added to the Department's advisory committees wherever possible, to enable them to have meaningful input at the early stages of policy development. These committees cover such diverse subjects as coastal zone management, energy, East-West trade, textile exports and imports, patents and trademarks, and economic development. Through contacts with consumer leaders and organizations throughout the country, nearly 40 consumer representatives for positions on various committees have been recommended. The third major element of the Commerce consumer program is the new Consumer Affairs Division created in June of 1976 in the Office of the Ombudsman, which, was already the Department's complaint handler and trouble-shooter for both business and consumers. One of the major activities is answering consumer inquiries and complaints, presently at the rate of about 2,500 per year. In many cases, we assist the consumer by conferring with or making them aware of their local resources for help--local government agencies, small claims courts, consumer action panels, etc. But in other cases, without enforcement authority, we have been quite successful in resolving complaints for which the consumer's own efforts or those of a local agency have failed.

To address this problem of unresponsiveness, the Office of the Ombudsman is sponsoring a series of Business-Consumer Relations Seminars throughout the country. The purpose of the seminars is to make businessmen more aware of current consumer concerns, and to encourage voluntary responsiveness to the needs of the consumer. Not only will this voluntary approach better serve the consumer directly, but it could contribute indirectly to reducing the amount of consumer legislation being passed.

Finally, the Consumer Affairs Division is actively involved in efforts to communicate with consumers throughout the country. We have an extensive mailing list of consumer agencies and organizations to whom we send our publications, and from whom we request input to various issues within the Department. We arrange meetings for consumer leaders with Commerce policy officials, and we are currently developing a plan for conducting consumer forums on major consumer-related issues in which the Department is involved.

In short, the Consumer Affairs Division role as "in-house consumer advocate" is to bring the views of the consumer into balance with those of business in policy and program decisions of the Department of Commerce. Further, the success of any business enterprise depends upon consumer satisfaction. Therefore, the Department's concern for consumer representation is an objective which ultimately is in the best interest not only of consumers, but of the business community as well.

CONSUMER REPRESENTATIVE IN THE FEDERAL RESERVE

Ms. Anne Geary*

The Federal Reserve Board is responsible for many consumer credit laws and regulations that directly affect consumers. Several of the laws and regulations are reviewed. A survey is currently being completed that will assist the Board in determining public awareness and attitudes toward consumer credit and consumer credit legislation.

The Federal Reserve Board's primary functions are managing the nation's money supply and supervising the safety and soundness of 1100 State chartered member banks. Although both these activities affect all consumers in the macroeconomics sense, the ordinary consumer probably has little interest in the lofty matters of monetary policy and international balance of payments. These matters do not have an immediate, day-to-day, or personal impact upon consumers. But the Fed is involved in consumer matters. The Division of Consumer Affairs is three years old with 50 employees.

The Federal Reserve has responsibility for several consumer protection laws. Four of these mandates are the Home Mortgage Disclosure Act, the Equal Credit Opportunity Act, Truth-In-Lending, and the Fair Credit Billing Act.

The HMDA is less than a year old--it went into effect in June, 1976. Consumer groups in urban areas concerned about the decay of inner city neighborhoods and the difficulty of obtaining loans on inner city property brought their complaints to the attention of Congress. The Congress responded with HMDA, which requires that once a year, depository institutions over a certain size prepare a statement showing by census tracts the location of property on which they have made mortgage loans. Depositors must be informed of the availability of the disclosure statements and the statements must be offered to anyone who requests thems. The purpose of the Act is to enable consumer groups and local officials to see where the depository institutions are lending, and to determine whether the institutions are serving the community's housing needs.

The Equal Credit Opportunity Act is another new law. It forbids discrimination in credit on the basis of race, color, religion, national origin, sex, marital status, age, receipt of public assistance benefits and exercise of rights under the Consumer Credit Protection Act. The implementing regulations outlaw certain discriminatory practices that were first identified by the National Commission on Consumer Finance. The Regulation

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prohibits creditors from discounting a wife's income and from asking an applicant for credit questions about his or her birth control practices or child-bearing capabilities. Creditors also are required to tell a consumer whether or not his application has been approved, and if an application is denied, to inform the applicant of the reason(s) for denial, either automatically or upon request. Another provision corrects the practice of reporting credit experience only in the husband's name, which had the result of creating a credit history only for the husband. The Board's regulations will now result in the creation of credit histories for married women. When those women are widowed or get divorced, or decide they want credit in their own names, they will not be in an adverse position.

Another law the Fed administers is Truth-in-Lending. This law, which was passed in 1968, is designed to promote the informed use of credit by enabling consumers to compare credit terms. The law requires creditors to disclose clearly, conspicuously, and in a meaningful sequence the sum of all charges the consumer must pay directly or indirectly for credit. Finally, the Fair Credit Billing Act provisions require creditors to tell consumers how to correct billing errors in their bills, and, of course, to correct the errors.

Thus, the Federal Reserve Board has responsibility for some important laws in the field of consumer credit. The Board wrote the implementing regulations as Congress directed, and the Fed interprets the laws. Creditors certainly know about these laws--the staff answers hundreds of letters each year from creditors who want to know what the law requires and whether a proposed course of action is permissible. With increasing frequency, we are wondering what the American consumer knows about consumer credit in general and these laws in particular.

Creditors mutter that laws such as Truth-in-Lending are a national disgrace, and that they should be drastically simplified or even repealed because they are complex, difficult to comply with, and costly. Creditors note that consumers do not shop for credit in 1977 any more than they did in 1967, and the first thing a consumer does with a Truth-in-Lending disclosure form is to throw it away. Is Truth-in-Lending a white elephant? Maybe the problem rests with lack of consumer awareness of the law. If that is so, what is needed is improved educational effort relating to consumer credit.

Six months ago at the direction of Congress, the Board established a Consumer Advisory Council. The Council is chaired by former Representative Leonor Sullivan, and composed of representatives of business and of the consumer interest. Education was the principal topic at the Council's last meeting. Several Council members had conducted informal, unscientific surveys in the areas to determine what primary and secondary students were being taught about consumer credit. Some school districts apparently offered no instruction in consumer credit. Some touched on the subject in home economics courses, where girls made up most of the enrollment. Of the schools that offered instruction in consumer credit, only a few required students to take the course.

The question the Board is asking itself is "What should the Board's role be?" As a first step, the Board has asked the University of Michigan's Consumer Research Center to conduct a survey on public awareness of credit laws and attitudes toward credit in general. The survey should give an idea of how serious the educational gap is, but it leaves unanswered the question of what the Board can and should do to close the gap. This is a concern that is well worth reviewing for all interested educators.

CONSUMER SATISFACTION WITH UTILITIES

Dr. William O. Bearden, Dr. Richard M. Durand,
Dr. J. Barry Mason, and Dr. Jesse E. Teel*

Demographic, psychographic, and media usage differences between complainants and noncomplainants regarding electric utility service are examined. Individuals most likely to complain were profiled as being younger, more educated, heavier consumers of print media, and generally more socially conscious. Electric utility management needs to prepare for an increasing number of complaints as individuals become more educated and incomes rise. Concern for the less educated and informed is also raised as these individuals may feel unable and powerless to affect utility policy.

Services now contribute approximately 50 per cent of the gross national product of the United States. This percentage will likely increase because of rising discretionary incomes, increasing participation of women in the labor force, and continued demand for activities oriented to life styles which require services such as education, personal care, and recreation. Yet, consumer satisfaction with services has received little research attention from academicians who have focused virtually all of their efforts on consumer concerns with tangible goods. However, increasing demand for services, e.g., medical services, legal services, education, and recreation, underscore the importance of service marketing. Furthermore, some services, including natural gas and electric utilities, are granted virtual monopolies by state and federal governments. Thus, it is imperative that research be conducted on both the quality of services and attendant consumer satisfaction with these services. This research will aid consumer affairs practitioners and academicians in providing input to regulatory policy-making bodies which will hopefully result in decisions more beneficial to both service agencies and consumers.

Although little information concerning consumer satisfaction/dissatisfaction with service industries exists, research has been done that deals directly with consumer complaints regarding durable products. A review of this research provides useful insight into the general dimensions of consumer dissatisfaction.

Various estimates of consumer dissatisfaction with durables indicate that approximately 50 per cent of consumers at any time are likely to be sufficiently dissatisfied to make some type of complaint.[1,2] Other studies suggest that this number may be even higher.[3] However, complaints deal with both products and services. Specific complaints frequently mention problems with repair, product safety features, home improvement, insurance and energy consumption.[4,5,6,7]

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Ralph Nader's Center for the Study of Responsive Law recently found that only 25 per cent of the problems people have with products are resolved to their satisfaction.[8] Anticipation of their failure to obtain redress apparently causes consumers to express their dissatisfaction to other consumers. Research has shown that people who get upset in the marketplace are most likely to complain personally to another consumer or else do nothing. If action is taken, it will most likely consist of a personal complaint to a store employee, e.g., manager, salesperson, or clerk.[9]

The literature to date provides other descriptive profiles of the dissatisfied consumer. For example:

> ....Evidence indicates it is the younger, more mobile, more educated consumer with a higher expectation, who is predominantly the "discontended consumer."[10]

> ....The average consumer complainer is a middle-age, well-educated, affluent, managerial-professional man or woman.[11]

> ....The demographic profile of discontented consumers indicates that the individuals most likely to operate effectively in the marketplace are those least content with its operation.[12]

Generally, research has profiled the chronic complainer as a person who contacts consumer protection agencies, newspapers, radio hotlines, and/or the FTC. The occasional or infrequent complainer is characterized as most likely to contact the retailer, the manufacturer, or the Better Business Bureau.[13]

Purpose of Research

The objectives of this research were to both determine the nature of consumer complaints about electric utilities and develop profiles of dissatisfied utility consumers. The expression of dissatisfaction with utilities is unique in that consumers are likely to experience more difficulty registering complaints about electric utilities than about tangible products. Consumers have less face-to-face contact with utility personnel than with retail store employees and may have to engage in overt search to register a complaint with a utility representative.

Methodology

The data were collected by means of structured personal interviews with 754 randomly selected respondents from a large southwestern community. Respondents provided information on the nature of their complaints about electric utilities in addition to individual demographic, psychographic, and media usage characteristics. The distribution of the sample's demographic characteristics indicated that the data were representative of the southwestern United States.

Twenty-nine statements on activities, interests and opinions (AIO's) were employed to measure respondents' psychographic (life style) characteristics. A principal axis factor analysis of these twenty-nine statements followed by a varimax rotation produced five general psychographic factors that explained 87 per cent of the variance in respondents' measured activities, interests and opinions. Based upon their component AIO variables, these factors were interpreted as representing groups of individuals who could be termed old-fashioned, outgoing/individualistic, service-quality conscious, fashion conscious and other-directed.

Media consumption information was obtained from respondents for local television stations, local radio stations, three weekly news magazines, and three daily newspapers. Radio and TV usage was defined as the total number of occasions that a respondent was exposed to a radio or TV station for at least fifteen minutes during the previous five day period, newspaper usage as the number of daily newspapers that each respondent read for at least 10 minutes over a five-day period, news magazine usage as the number of weekly magazines that each respondent read for at least 10 minutes per week over a four-week period.

Complaints were identified from their response to the following question:

> Have you written, called, or spoken to a representative or employee of _________ company over the last six months...

Those consumers providing positive responses were asked to describe the nature of their specific complaints. Complainants were then compared with noncomplainants along demographic, psychographic, and media dimensions by t-tests of mean differences and chi-square tests of categorical groupings.

Results and Discussion

Eighty respondents were identified as complainants regarding electric utility services. The nature of specific individual complaints were reflected in the following percentages: (1) 37.7 per cent - excessively high monthly bill; (2) 12.5 per cent - problem with bill; (3) 3.8 per cent - overdue bill; (4) 6.3 per cent - electric service interrupted; (5) 6.3 per cent - requests for restoration of service; and (6) 33.4 per cent - other varying or forgotten reasons.

With respect to demographic variables, complainants tended to be (1) younger, (2) better-educated, (3) wealthier, (4) responsible for more pre-school children, and (5) more likely to own their own home than non-complainants. Further, complainants exhibited more fashion consciousness than noncomplainants.

The differences in media exposure patterns of complainants and noncomplainants indicate that complainants read more news magazines and listen to more radio than noncomplainants. Complainants tended to watch television less and read the newspaper more than noncomplainants although these two differences were not statistically significant. These findings support the accepted demographic and psychographic profile of complainants as individuals who are heavier consumers of print media and thus better informed and possibly more articulate than noncomplainants.

Conclusions and Implications

These results support earlier findings in that individuals found to complain regarding electric utility service appear to be similar to those individuals who have been shown to complain regarding tangible consumer products in other studies.[14,15,16] While the electric utility complainant segment within any area may represent a relatively small percentage of all utility customers, a vocal minority this size easily could impact marketing utility policies. The unique profile of these individuals also suggests other definite implications for electric utility managers in their dealings with the consuming public.

As incomes rise and individuals become more educated and informed, management of electric utility companies can expect substantial increases in the number and frequency of individual complaints. Also, as incomes rise, individual expectations for a higher standard of living increase. However, rising costs and demands on electric utility facilities coupled with environmental and shortage concerns will restrict any improvements in service, which will certainly affect consumer feelings of satisfaction.

The relative size of the specific complainant consumer segment found in this study is probably even substantially underestimated. First, the noncomplaints in this analysis included those individuals who provided nonsubstantive respondents (e.g., no opinion or "don't know"). Second, those most affected by poor service and rising costs are the less informed, less educated, and lower income individuals. However, these are the consumers who are also most likely to feel overshadowed, and hence not complain, in their dealings with electric utility companies. Management needs to implement policies which would insure the availability of complaint procedures to the more disadvantaged.

Finally, most complaints isolated in this study dealt with some aspect of billing procedures. Further efforts need to be directed toward assessing if these problems are valid or whether the concerns are characteristic of the individuals involved. Future research needs also to examine varying communication strategies that might be useful in answering consumer complaints and in disseminating electric utility policy and usage information.

FOOTNOTES

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13. Joseph B. Hair, Rolph Anderson, and Paul Busch, "Profiling the Complaining Consumer: A Cluster Analysis Approach," In Howard C. Schneider (Ed.), 1976 American Institute for Decision Sciences Proceedings, p. 313.

14. J. T. Liefield, F. H. C. Edgecombe, and Linda Wolfe, op. cit., pp. 73-80.

15. William Lundstrom and Roger Kerin, op. cit., p. 312.

16. John A. Miller, op. cit., pp. 65-84.

STATE INSURANCE COMMISSIONERS AND THE CONSUMER PROTECTION FUNCTION

Dr. August Ralston*

The paper is based on the premise that there is an ill-defined regulator-insurance consumer relationship which hinders effective regulation by the state insurance departments. The purpose of the paper is to: (1) examine the current status of direct insurance consumer protection (DICP), (2) evaluate insurance consumer awareness of services provided by a state insurance department, and (3) present arguments for expansion of the DICP function.

Introduction

William Jennings Bryan offered his views on many topics. Insurance regulation was not an exception. In a speech, he observed:

> You will find that in every subject there is a fundamental proposition..., you will find that there is one fundamental principle that underlies irrigation; it is that water runs down hill. The man who tries to establish an irrigation plant without knowing that is going to have difficulty.[1]

Relating this observation to insurance regulation, he stated:

> There is a principle in insurance that is just as fundamental as that experienced in irrigation, and that is that security is the one thing that is important above all other... All the efforts of the State are directed toward the security of the insured... Gambling is the antithesis of security, and the efforts of legislation and administration is to take insurance out of the gambling class and put it into the certainty class. That is all there is to it.[2]

The reasons for and approaches to insurance regulation may be more numerous and complex than suggested by Mr. Bryan. However, he accurately identified the emphasis that has evolved and dominates insurance regulation. Through capital, reserve, surplus, and investment requirements enforced by disclosure and examination, the states attempt to create a reasonable certainty that insurers will be able to meet their financial obligations to policyholders and third party claimants. In addition to this emphasis on solvency regulation, the state insurance departments concentrate on premium rate regulation, insurance agent licensing, and policy form approval.

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The above elements combine to give the insurance regulatory structure a basic characteristic. It is indirect with respect to the insurance consumer. The basic components do not require the regulator to communicate with consumers through either direct contact or the providing of useful information. In the existing structure, there are strong, well-defined regulator-insurer and regulator-agent relationships, but there is a weak, ill-defined regulator-insurance consumer relationship.

Activities which require communication between insurance regulators and consumers may be defined as direct insurance consumer protection (DICP). DICP as defined here does not include all policyholder treatment aspects of regulation. It is limited to those activities which bring the regulator and the consumer into contact.

DICP is not nil. For example, many state insurance departments offer consumer services such as procedures for policyholders and claimants to register complaints and the distribution of information booklets. However, insurance commissioners as a group have placed a low priority on DICP. As a result, DICP is fragmented and of limited scope, virtually isolating the insurance consumer from the regulator.

Purpose

The purpose of this paper is to: (1) examine the current status of DICP and the focus of insurance regulation in the consumerism movement, (2) evaluate insurance consumer awareness of services provided by a state insurance department, and (3) present arguments for expansion of the DICP function. There is no intent to suggest that DICP is more important than or should be practiced to the exclusion of indirect regulation. The supposition is that insurance regulation is not whole with the benefits derived from effective indirect regulation. Further, the emphasis on indirect regulation has hindered state insurance departments in realizing their potential as complete insurance consumer protection agencies which are visible to the consumer.

Status of Insurance Consumer Protection

There is evidence that insurance regulators are becoming more concerned with the consumerism aspects of insurance regulation. This trend is well described by the following quote:

> Heretofore, ... , direct contact between commissioners and the consumer was relatively infrequent and then usually only on an individual basis, such as when a policyholder made a complaint. When a regulator spoke out on a subject of importance, he generally did so before a trade association, in the trade press, or at a legislative hearing. Lately, however, more and more commissioners have been trying to deal more directly and formally with the individual consumer and with "organized consumers."[3]

The DICP Function

The status of the DICP function within the consumerism movement was summarized in a recent study.[4] The insurance commissioners were surveyed to determine the types of consumer services offered by their departments. The responses are presented in Table 1.

Table 1

Consumer Service Category		Number of States
Complaint service only		19
Informational booklets		10
Toll-free hotline		3
Newspaper columns		1
Booklets and hotline		3
Hotline and newspaper columns		1
	Total	37

The basic component of DICP is the complaints service. All insurance departments are open to hearing complaints from insurance consumers. The data in Table 1 suggest a somewhat limited scope for DICP beyond the handling of complaints. Over one-half of the 37 respondents confine their involvement to the complaints service. The providing of informational booklets is the most prevalent form of DICP to augment the complaints function. Only a few states make a toll-free hotline available to insurance consumers and distribute information through newspaper columns. The most frequently cited reason for not initiating more DICP efforts is budgetary constraints.

The Current Thrust

In the consumerism movement, more attention is being given by insurance regulators to the question of policyholder treatment. However, because of the form that the current thrust is taking the role of DICP in the movement is unclear.

Identification of Regulatory Imbalance

The 1974 "New York Report on Regulation of Financial Conditions of Insurance Companies" stimulated interest in the need to give more attention to policyholder treatment. The Report disclosed that of the time spent in examining insurers, for domestic life insurers, 22.2 per cent was devoted to policyholder treatment aspects. For domestic non-life insurers, the per cent was 16.3.[5] This data caused the department to question whether it was allocating its resources efficiently in view of consumer expectations. The Report concluded that it is no longer appropriate to regard the prevention of insolvency as the absolute goal of insurance regulation. "Instead, the regulatory objective of sound financial condition must increasingly be balanced against its impact on other, perhaps more important, goals related to improved market performance."[6]

The National Association of Insurance Commissioners (NAIC) is participating in the movement toward giving greater attention to policyholder treatment. The McKinsey Study,[7] commissioned by the NAIC, identified two ultimate purposes of surveillance or insurance company examinations: first, to protect against insolvencies and, second, to ensure fair treatment of policyholders and claimants.[8]

In considering the deficiencies in the present examination system, the Study concluded that "... the procedures that do exist focus almost exclusively on financial condition; procedures for evaluating the treatment of policyholders and claimants are virtually nonexistent."[9] Further, regarding the emphasis on financial condition:

> (The examination system) allocates most of the man-months spent in examination of financial conditions to companies that are least likely to have solvency problems. ..., in the past 5 years, over 60 per cent of examination man-months has been spent on companies with premium income of over $25 million, even though there have been no insolvencies among companies of that size during the past 10 years.[10]

Market Conduct Surveillance System

The remedy recommended by the Study to intensify the regulatory attention given to the fair treatment of policyholders and claimants is to divide the examination system into two parts as follows:

1. <u>A financial condition surveillance system</u>, which will focus on a company's financial soundness.

2. <u>A market conduct surveillance system</u>, which will focus on a company's practices in sales and advertising, rating, underwriting and claims handling.[11]

The purpose of the market conduct surveillance system (MCSS) is to protect policyholders and claimants against unfair sales, advertising, underwriting, rating, and claims practices.[12] The key elements in the MCSS are:

1. a complaint analysis system that identifies the problem companies and the problem lines of business in the state,

2. a system for scheduling targeted field examinations, and

3. field examination procedures tailored in scope and depth to the nature of the company's operations and the problems at issue.[13]

The MCSS is a positive development for insurance consumer protection and may lead to expanded DICP but there are reservations. It is in the early stages of implementation and no state is compelled to adopt the system. Also, the procedures set out in the recently drafted Market Conduct Examination Handbook will not necessarily bring about a stronger regulator consumer relationship.

The Handbook calls for the evaluation of market conduct to be primarily based on a sampling of pertinent information on file with state insurance departments, such as complaints, rating, and policy form information.[14] The commissioners may find that their existing information is inadequate for effective market conduct surveillance. For example, the complaints on file may not be a sufficient data base if a significant number of consumers who have complaints do not in fact register them. Therefore, regulators will establish lines of communication with policyholders and claimants to gather needed information and thereby promote DICP only in proportion to their desire for MCSS to be effective.

Consumer Awareness of the Insurance Department Consumer Protection Function

A Recent Study of Consumer Perception

In the recent Wharton Study,[15] the researchers asked each individual sampled: How would you rate the job the Federal Government, the state government, local government, and private consumer protection groups do in protecting consumers' rights on insurance?[16] The responses are summarized in Table 2. In analysing the ratings, the authors note:

> If the response "excellent" or "pretty good" is termed positive and "only fair" or "poor" is negative, then only private consumer groups receive more positive responses than negative ones (33 per cent positive versus 32 per cent negative) and even for this category 35 per cent are not sure how good a job such groups are doing.[17]

Table 2

Agency	Per cent of Respondents by Rating Indicated				
	Excellent	Pretty Good	Only Fair	Poor	Not Sure
Federal government	3.4	29.5	29.2	14.6	23.2
State government	4.4	34.1	29.1	12.0	20.5
Local government	2.9	24.3	24.9	18.3	29.6
Private consumer protection groups	4.6	28.7	21.2	10.7	34.7

Source: J. David Cummins, Dan M. McGill, Howard E. Winklevoss, and Robert A. Zelten, Consumer Attitudes Toward Auto and Homeowners Insurance. (Department of Insurance, Wharton School-University of Pennsylvania, 1974), p. 204.

The fact that the negative responses outweigh the positive responses for all government categories is informative in evaluating consumer perception of the effectiveness of various agencies in protecting their rights on