Legal MATTERS

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Treating Customers Fairly: The Roadmap

Source: FSB. Treating Customers Fairly, The Roadmap. 31 March 2011

Chapter 1: Roadmap purpose and structure

The FSB has published a roadmap to inform financial services stakeholders of the approach that it intends to adopt in implementing a "Treating Customers Fairly" approach in South Africa.

The roadmap provides an overview as to why the FSB will be introducing the TCF model; the desired outcomes of TCF; and a summary of where TCF fits into the FSB's broader market conduct regulatory mandate.

Chapter 2: An overview of TCF – The desired outcomes of TCF

TCF is a regulatory approach that seeks to ensure that specific, clearly articulated fairness outcomes for financial services customers are demonstrably delivered by regulated financial institutions.

The six fairness outcomes

- **Outcome 1:** Customers are confident that they are dealing with firms where the fair treatment of customers is central to the firm's culture.
- **Outcome 2:** Products and services marketed and sold in the retail market are designed to meet the needs of identified customer groups and are targeted accordingly.
- **Outcome 3:** Customers are given clear information and are kept appropriately informed before, during and after the time of contracting.
- **Outcome 4:** Where customers receive advice, the advice is suitable and takes account of their circumstances.
- **Outcome 5:** Customers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and what they have been led to expect.
- **Outcome 6:** Customers do not face unreasonable post-sale barriers to change product, switch provider, submit a claim or make a complaint.

TCF will require regulated firms to consider their treatment of customers at all stages of their relationship with the customer, from product design and marketing, through to the advice, point-of-sale and after-sale stages.

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Ultimate desired outcomes of TCF

- Improved customer confidence
- The supply of appropriate products and services, and
- Enhanced transparency and discipline in the industry

Chapter 3: A structural model for delivering TCF

The TCF model will consist of three main “pillars”. (Pillar 1: The TCF Framework; Pillar 2: Implementing TCF; Pillar 3: Incentives & Deterrence). Each of the pillars will place specific obligations on the FSB and firms respectively.

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Chapter 4: Pillar 1 - The TCF framework

A regulatory framework is required to ensure that firms deliver the desired outcome referred to above
Aims of the regulatory framework

- Consistency: The framework must be developed to deliver consistently fair outcomes for customers across the retail financial sectors that the FSB regulates.

- Completeness*:* The framework will need to close gaps in existing consumer protection coverage and review any elements of existing regulation that may present obstacles to the fairness outcomes.

- Co-ordination*:* The framework will require effective co-ordination of legislative reviews of sector specific financial legislation, to reduce the risk of duplication, inconsistencies or gaps in regulation.

- Alignment with international best practice: The framework illustrates a commitment to international regulatory best practice.

Stakeholder engagement
The FSB will engage with affected stakeholders, ombud schemes, regulatory experts and other authorities to obtain input and support in developing the TCF regulatory framework.

Regulatory themes
There will be a focus on a number of regulatory themes aligned to the fairness outcomes as set out in Chapter 2. These themes are:

- TCF culture
- Appropriately targeted design and marketing of products and services
- Clear information
- Suitable advice
- Products perform as expected and acceptable service
- No unreasonable post sale barriers.

Regulatory alignment analysis
Once the regulatory themes have been more fully described, an analysis of legislation will be undertaken to identify gaps and inconsistencies between:

  - The various existing provisions themselves in relation to TCF related matters and
  - The existing provisions and their likely effectiveness in delivering the TCF fairness outcomes.

Both FSB supervised legislation and legislation supervised by other government departments (to the extent relevant to achieve the TCF outcomes) will be analysed.

The FSB will develop a TCF supervisory framework
Aims of the supervisory framework

An effective TCF supervisory framework must be:

- Risk-based and proportional*:* The TCF supervisory approach must be structured to ensure that firms and sectors posing a proportionally greater risk of unfair customer treatment are subject to more intensive supervision than those posing a lower market conduct risk.
- Proactive and pre-emptive*:* The FSB will need to build additional capability to monitor (and communicate) emerging conduct risks and undesirable trends.
- Intensive and intrusive: Oversight will need to be more intensive and intrusive than has been the case historically – albeit in a risk-based manner.

Enhanced supervisory techniques and capacity
The FSB's approach to reporting and off-site and on-site monitoring will be reviewed to ensure that the supervisory framework can achieve the aims outlined above.

Chapter 5: Pillar 2 – Implementing TCF

A new culture and governance approach by regulated firms
The primary responsibility of firms in implementing TCF will be to demonstrate achievement of the first of the fairness outcomes that the fair treatment of customers is central to the firm's culture.

Embedding a TCF culture
Implementing TCF will not be a once-off event within a firm, but must become an ongoing, evolving and ultimately permanent feature of a firm's approach to its business.

A TCF culture framework
Firms will be expected to build a TCF approach into:

- Leadership: The Board, senior and middle management need to provide direction and monitor the delivery of TCF behaviours and outcomes.
- Strategy: The TCF aims need to be carried through to implementation as part of the firm's broader business strategy.
- Decision-making: Decision-making protocols should ensure that decisions are tested for customer impact.
- Governance and Controls: The governance structures and control mechanisms within firms will need to be designed to create disciplines around TCF.
- Performance management: The recruitment of appropriate staff and representatives, trained to deliver appropriate TCF outcomes, is necessary. TCF deliverables should form part of staff performance contracts where appropriate and performance should be evaluated in terms of TCF competence and expectations.
- Reward: Remuneration, incentive and reward policies need to take cognisance of fair customer outcomes and entail consequences for TCF successes and failures.

The FSB will adopt an intrusive approach to supervision which will result in an enhanced, more proactive and intensive supervisory approach to enable pre-emptive identification of market conduct risks.

CHAPTER 6: Pillar 3 – Incentives & deterrence

This pillar of the TCF framework involves application of positive and negative incentives to encourage commitment by regulated firms to achieving the TCF outcomes.

Action by regulated firms
In order for the FSB to enforce delivery of TCF outcomes, it must be in a position to monitor such delivery which could be achieved by disclosure and reporting requirements.

Public disclosure of identified TCF performance measures
Through correctly structured public reporting, a measure of market discipline is envisaged. Firms who perform well on publicly disclosed TCF measures should gain market competitive advantages as a result of positive public perceptions.

Non-public reporting as required by the FSB
Over and above any publicly reported TCF measures, the FSB will require extensive reporting on TCF measures and practices.

Action by the FSB
Enforcement mechanisms for credible deterrence
For TCF to achieve its desired outcomes, firms must know that the regulator is in a position to enforce firms' TCF accountabilities.

Pre-emptive intervention for industry conduct risks
Where risks are identified, the FSB will need to take action to mitigate these risks to prevent or minimise harm to consumers.

Pre-emptive intervention for firm specific conduct risks
The FSB will need to take action to mitigate these risks to prevent or minimise harm to consumers. Depending on the seriousness of the identified risk, this could entail immediate regulatory action or engagement with senior management to reach agreement on the necessary course of action.

Formal regulatory enforcement action
Where an agreed course of action to mitigate conduct risks, as described above, would not be effective or appropriate, the FSB will take formal enforcement action against firms and / or individuals responsible for TCF failures.

"Name and shame"
The reputational consequences for firms of public disclosure of their TCF successes and failures, introduces market discipline into the TCF framework. Similarly, the risk of public disclosure of TCF enforcement action being taken against a firm should be an effective deterrent of unfair customer treatment.

Chapter 7: Support structures

The three pillars of the TCF framework: The TCF framework, implementing TCF, and the measures required to incentivise TCF and deter unfair treatment of customers are supported by a range of other policy initiatives, involving other financial services stakeholders. The main support structures for TCF are:

- the role of ombud schemes in delivering "ultimate fairness" to financial consumers;
- the underpinning of the broader national consumer protection frameworks through complementary and co-ordinated measures of other regulators; and
- ensuring that customers are empowered to demand fair treatment through consumer education and awareness initiatives.

"Ultimate fairness" through ombud schemes
It is essential that customers have ready access to simple and effective alternative dispute resolutions mechanisms. In the financial sector various statutory and voluntary ombud schemes provide this access.

Regulatory co-ordination and information sharing
There is a need to promote greater co-ordination and information sharing between all financial regulators (including international regulators) and establish a Council of Financial Regulators. Regulatory co-ordination and information is vital in order to ensure that

- market conduct regulation and prudential regulation complement each other to in order to provide a safer financial services sector; and
- the market conduct regulation itself achieves its aim of consistency, completeness and co-ordination.

Consumer education and awareness
The delivery of TCF will be strengthened if customers are aware of:

- their right to fair treatment;
- the regulators expectations of firms in this regard;
- the recourse available to them in the event of unfair treatment.

The FSB will therefore drive consumer awareness of TCF as part of its broader consumer education initiatives.

Next steps and time frame

TCF self-assessment tool
The FSB is in the process of developing a self-assessment tool, which regulated firms can use to gauge their success levels in achieving the TCF fairness outcomes and culture framework requirements.

Structure of the self-assessment tool
The self-assessment tool will take the form of a questionnaire, structured around each of the six fairness outcomes, with particular emphasis on the elements of the TCF culture framework.

Purpose
In addition to assisting firms in assessing their TCF competency levels, the self-assessment tool is intended to provide firms with a high level indication of the kinds of factors the FSB will in future take into account in monitoring and assessing TCF compliance, once the TCF supervisory framework is implemented.

Piloting the self-assessment tool
Once the draft self-assessment tool has been finalised, the FSB will pilot it with a number of regulated firms before making it generally available for industry use. Approximately 20 to 25 firms will be invited to participate in the pilot project. Participants will be representative of the entire financial services sector excluding small and medium sized category 1 financial services providers. The intention is to identify participants and to provide them with the self-assessment tool by June 2011 and to conduct follow up interviews by July 2011. Thereafter a revised tool will be distributed to the industry by August 2011.

Limitations of the self-assessment tool
Although the self-assessment tool may serve a useful purpose in aiding TCF implementation and understanding, it cannot serve as a definitive ‘template’ to guarantee full compliance with TCF accountabilities. Firms should develop their own self-assessment measures and rely on the FSB’s tool as guidance where appropriate.

The TCF benchmarking exercise
After the TCF self-assessment tool has been piloted and published for industry use and guidance, the FSB will therefore conduct a benchmarking exercise, using the self-assessment tool. The sample size of the benchmarking exercise must still be determined but the aggregated results will be publicly available. The aim is to commence with the benchmarking during August and September 2011 and to publish the results in early 2012.

Stakeholder engagement strategy
A TCF Regulatory Framework Steering Committee will be established, with suitable representatives from:

- Regulated industry sectors. (Industry associations will be approached to assist the FSB in identifying suitable participants).

- Other financial market conduct regulatory agencies and ombud schemes.
- The National Treasury.
- Independent experts on consumer and regulatory matters, if necessary.
- The aim is to have the Committee in place by end May 2011. Working groups will be established under the oversight of the Committee.
- The aim is to provide a regulatory framework proposal to National Treasury for their approval during the last quarter of 2012. The normal consultation and approval processes will thereafter be followed before the final legislation is to be published. These timelines do not preclude earlier implementation of TCF related regulation necessitated to addresss market conduct concerns.
- The aim is to to fully implement the regulatory framework legislative changes by January 2014.