Regulatory Intelligence

Updating you on current insurance regulatory developments

The FSB is implementing a programme for regulating the market conduct of financial services entities to ensure the fair treatment of customers is embedded within the culture of financial entities.

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In February 2011 National Treasury published a document entitled "*A safer financial sector to serve South Africa better*". One of the key policy priorities of financial regulation identified in the document is consumer protection and market conduct. In terms of the document South Africa will move towards a "twin peaks" model of financial regulation – one regulator tasked with prudential regulation and another tasked with market conduct regulation. The Financial Services Board (FSB) has been tasked with the responsibility of market conduct regulation.

As part of fulfilling this responsibility the FSB is implementing its Treating Customers Fairly (TCF) initiative. TCF aims to regulate market conduct of financial services entities to ensure that fair treatment of customers is embedded within the culture of these entities.

Entities usually have more expertise and resources available in designing, distributing and servicing financial products, than consumers have available to them in making decisions about transacting with such entities. For this reason consumers need more protection against unfair practices. TCF therefore aims to develop a holistic and co-ordinated consumer protection regulatory framework that applies consistently across all financial services entities.

The FSB issued a Discussion Paper in April 2010 examining the elements of the TCF programme and to consider its application in South Africa. The discussion paper looked at a "principles and rules-based approach" to compliance.

On 31 March 2011 the TCF Roadmap was issued by the FSB. The Roadmap's purpose is to inform financial services stakeholders of the approach the FSB intends to adopt in implementing TCF.

Desired outcomes of TCF

The TCF Roadmap identifies 6 outcomes which need to be achieved through the implementation of the TCF framework. These are:

1) Customers are confident that they are dealing with entities where the fair treatment of customers is central to the entity's culture;

2) Products and services are designed to meet the needs of identified customer groups and are targeted accordingly;

3) Customers are given clear information and are kept appropriately informed before, during and after the time of contracting;

4) Where customers receive advice, the advice is suitable and takes account of their circumstances;

5) Customers are provided with products that perform as entities have led them to expect;

6) Customers do not face unreasonable post-sale barriers to change products, switch provider, submit a claim or make a complaint.

TCF is also expected to deliver intermediate outcomes being:

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

TCF at each stage of the product life cycle

In order to achieve the core outcomes of TCF, the cultural and operational aspects of entities will need to change.

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Financial services entities will be required to demonstrate that they consistently treat customers fairly throughout the stages of the product life cycle:

Product and service design:

Products and services, including the distribution strategies, should be designed and developed for a specific target market, based on a clear understanding of the likely needs and financial capability of the customers.

Promotion and marketing:

Products should be marketed through clear and fair communications that are not misleading to the targeted customers.

Advice:

Advice should be suitable to the needs of the customer concerned.

Point-of-sale:

Clear and fair information should be provided to enable customers to make informed decisions.

Information after point-of-sale:

Entities should provide customers with ongoing and relevant information to enable them to monitor whether the products or services continue to meet their needs and expectations.

Complaints and claims handling:

Representations, assurances and promises that lead to legitimate customer expectations should be honoured.

Structural model to deliver TCF

The TCF model will consist of three main pillars, each of which will place specific obligations on financial services entities and the FSB respectively.

Pillar 1: The TCF Framework

TCF is guided by the 6 fairness outcomes outlined above, but experience has shown that relying on principles alone does not drive the behavioural and culture change envisaged in TCF. Therefore the principles are augmented with a regulatory framework which will balance principles-based and rules-based regulation.

The TCF framework will aim to achieve:

- Consistent delivery of fair outcomes for customers;
- Closing gaps in existing consumer protection coverage and regulation;
- Co-ordination of legislative reviews of sector specific financial regulation; and
- Alignment with international best practice.

The supervision of the regulatory framework will require an appropriate supervisory framework to which the FSB will adhere.

Pillar 2: Implementing TCF

Fair treatment of customers must become the central focal point to the entity's culture. To achieve this financial services entities will need to focus on the TCF outcomes at all stages of the product life cycle as well as at all levels of planning, decision-making, management and operations within the entity. TCF cannot be seen as a once-off event, but an ongoing, evolving feature of the entity's approach to business.

Entities will be required to demonstrate their compliance with the TCF framework and development of a TCF culture. This implies that management information to monitor and measure the entity's performance against the outcomes will need to be developed.

The FSB has indicated that reporting mechanisms will be developed as part of the supervisory framework to assist the FSB in assessing the extent to which TCF has been embedded within an entity's culture. Such reporting is likely to include both public and non-public disclosures integrated within existing returns. On-site and off-site supervision is being proposed by the FSB to allow the FSB to assess and evaluate the information available.

Pillar 3: Incentives and deterrence

The approach to incentives and deterrence will require entities to be able to provide clear information on their TCF performance and require the FSB to analyse and respond to such information. Possible public disclosures include claims statistics measures, complaints volumes, adherence to service levels and

investment performance. It is envisaged that the reputational impact of such disclosure may act as a powerful deterrent of unfair customer treatment and as an incentive for entities to compete over the quality of customer experiences.

The FSB will carry the obligation of enforcing TCF accountability on entities. This may take one of the following forms:

- Pre-emptive interventions to mitigate industry conduct risks and minimise harm to consumers. This may include engagement with appropriate industry associations, issuing specific guidance, on-site visits to affected entities, publishing warnings or other guidance for consumers or introducing new regulations.

- Pre-emptive interventions for entity-specific conduct risks. This is likely to involve engagement with senior management to reach agreement on a course of action that ensures that the identified unfair treatment stops, etc.

Where the above actions would not be effective or appropriate, the FSB may take formal enforcement action against entities for TCF failures. These may include administrative fines or penalties, suspension or withdrawal of licences, referral of matters to the High Court.

The FSB will also consider a "name and shame" approach to less formal regulatory interventions and enforcement action taken against entities.

Support structures

Supporting these three pillars are the following support structures:

- The role of the ombud schemes in delivering fairness to financial consumers;

- The national consumer protection frameworks and co-ordination with other regulators; and

- Ensuring that customers are empowered to demand fair treatment through consumer education and awareness.

Next steps in the TCF process

Financial Services entities are encouraged to take part in the next steps of the implementation of TCF and to adopt and develop a TCF self-assessment tool, engage with the FSB on the results of the benchmarking exercise in August 2011, and to formally develop a stakeholder and customer communication strategy with respect to TCF.

Conclusion

The embedding of the TCF framework is expected to involve significant resource, time and operational change for financial services entities in South Africa. A review of current practices throughout the product life cycle should be performed to identify gaps in the entity's customer strategy and to embed the culture of TCF within the entity.

If you wish to discuss how we can help you, please call your regular contact or alternatively:

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