



# Treating Customers Fairly

## The Roadmap

March 31

# 2011

The Financial Services Board is implementing a programme for regulating the market conduct of financial services firms, entitled Treating Customers Fairly (TCF). The TCF approach seeks to ensure that fair treatment of customers is embedded within the culture of financial firms. TCF will use a combination of market conduct principles and explicit rules to drive the delivery of clear and measurable fairness outcomes, and will enforce the delivery of these outcomes through imposing a range of visible and credible deterrents to unfair treatment.

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# CHAPTER 1:

## Roadmap purpose and structure

The purpose of this Roadmap is to inform financial services stakeholders of the approach the Financial Services Board (FSB) intends to adopt in implementing a “Treating Customers Fairly” approach to the market conduct regulation of retail financial services in South Africa.

It also responds to the feedback which stakeholders provided to the TCF Discussion Document issued for comment by the FSB in April 2010.

The Roadmap is structured as follows:

### **Chapter 2: Overview of TCF**

Chapter 2 provides an overview of 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, as set by the National Treasury’s financial sector regulatory policy. The six “fairness outcomes” that firms will be expected to achieve for their customers are presented and explained in terms of the financial product life cycle. The vision, or ultimate outcome, of the TCF programme for the FSB is that customers’ financial services needs are appropriately met through a sustainable industry. This embraces the following outcomes of TCF: Improved customer confidence, appropriate products and services, and enhanced transparency and discipline.

### **Chapter 3: A structural model to deliver TCF**

Chapter 3 provides a structural model for TCF, made up of 3 Pillars and a number of supporting structures. Each pillar requires specific deliverables from regulated financial services firms and the FSB respectively. Pillar 1 is the TCF framework, consisting of a regulatory framework and a supervisory framework. Pillar 2 sets out the implementation requirements for the TCF framework outlined in Pillar 1, being a new approach to culture and governance by regulated firms, and an enhanced approach to supervision by the FSB. Pillar 3 provides for incentives and deterrence mechanisms to drive the successful implementation of TCF, addressing disclosure and reporting obligations for firms and enforcement mechanisms to be used by the FSB. The three pillars are supported by structures involving other stakeholders: Ultimate fairness through ombud schemes, co-ordination and information sharing with other regulators, and consumer education and awareness initiatives.

## **Chapter 4: Pillar 1 – The TCF framework**

The formal TCF framework making up Pillar 1 of the TCF model, will comprise a regulatory framework within which firms will be required to conduct business, and a corresponding supervisory framework to be developed by the FSB. Chapter 4 outlines the aims and features of the TCF regulatory framework and summarises the process to be followed in developing the regulatory framework. The process will include stakeholder engagement, identification of regulatory themes for TCF and a regulatory alignment analysis to identify gaps, inconsistencies or overlaps in existing legislation. Chapter 4 also provides further detail of decisions that will need to be taken in finalising the intended scope of the regulatory framework. Chapter 4 goes on to set out the aims and requirements of the TCF supervisory framework that the FSB will develop to oversee the regulatory framework.

## **Chapter 5: Pillar 2 – Implementing TCF**

Chapter 5 focuses on the changes in approach that Pillar 2 will require from both firms and the FSB to successfully implement Pillar 1's TCF framework. Firms will need to make cultural and governance changes to ensure that a TCF culture is fully embedded in their organisations, and the chapter sets out the components of a TCF cultural framework. The FSB will be required to adopt an enhanced, more proactive and intensive supervisory approach to enable pre-emptive identification of market conduct risks. The chapter outlines the broader reporting and monitoring strategies that will be implemented.

## **Chapter 6: Pillar 3 – Incentives and deterrence**

Chapter 6 deals with the mechanisms that will be used to reinforce commitment to the TCF outcomes and to discourage unfair customer treatment. Firms will have to comply with non-public FSB reporting requirements to enable the FSB to carry out intensive conduct supervision. They will also have to publicly report on various TCF success measures, aimed at instilling an element of market discipline and competitive pressure into TCF delivery. The chapter also sets out a range of enforcement measures that the FSB will have at its disposal to ensure credible deterrence of TCF failings.

## **Chapter 7: Support structures**

The 3 Pillars of the TCF structural model will be supported by a number of support structures, involving other stakeholders. Chapter 7 summarises the way in which the implementation of TCF will entail engagement with relevant financial services ombud schemes to ensure "ultimate fairness", co-ordination and information sharing with other market conduct regulators and synergies between TCF and longer term consumer education and awareness initiatives.

## Chapter 8: Next steps

Chapter 8 sets out the immediate next steps the FSB will be undertaking in rolling out TCF. These include developing and piloting a TCF self-assessment tool for use by regulated firms, conducting a TCF benchmarking exercise and setting up the stakeholder engagement structures required to develop the TCF regulatory framework and other elements of the TCF model.

## Chapter 9: TCF timeline

Chapter 9 contains a timeline setting out target dates for key milestones in the TCF implementation, over a period of approximately three years.

## **Annexure A: Review and feedback on comments received on the FSB's "*Treating Customers Fairly*" Discussion Document (April 2010)**

This annexure provides a summary of the main categories of feedback and comment submitted by stakeholders in response to the TCF Discussion Document published by the FSB in April 2010. It also provides the FSB's responses to the most significant comments and concerns, mainly with reference to the relevant sections of the main body of this Roadmap.

# CHAPTER 2:

## An overview of TCF

### Why TCF?

The asymmetry of information between retail financial services consumers and financial institutions means that financial services consumers are particularly vulnerable to unfair treatment. Typically, financial institutions have far more expertise and resources available to them in designing, distributing and servicing financial products than consumers have available to them in making decisions about financial transactions. The nature of financial products and services is such that, in many instances, the consequences of unfair treatment or poor decisions are only felt some time – in some cases many years – after transacting. Significant hardship can result. In South Africa, these challenges are exacerbated by low levels of both basic and financial literacy, increasing the risk of consumer exploitation.

South African financial sector regulation includes various measures aimed at protecting consumers of financial products and services<sup>1</sup>. Although these have proven useful in mitigating various specific risks to consumers, a holistic and co-ordinated consumer protection regulatory framework that applies consistently across the financial services sector – and is tailored to address the specific conduct risks peculiar to the sector – has been lacking.

Against this background, in April 2010, the Financial Services Board (FSB) published a discussion document entitled *Treating Customers Fairly (The TCF Discussion Document)*. The motivation and intended outcomes of TCF were set out, together with a brief history of the TCF approach as implemented by the Financial Services Authority (FSA) in the United Kingdom. The TCF Discussion Document indicated that TCF would be adopted as part of the South African regulatory framework. The TCF Discussion Document also highlighted some practical examples of potential application of the TCF approach in South Africa. Stakeholders were invited to submit comment on the proposals.<sup>2</sup>

This Roadmap confirms the commitment of the FSB to the TCF programme by setting out its approach to implementation.

### The desired outcomes of TCF<sup>3</sup>

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.

<sup>1</sup> See Chapter 4 for a discussion of existing financial consumer protection legislation.

<sup>2</sup> Comments received and the FSB's responses are summarised in Annexure A.

<sup>3</sup> This section is taken from the TCF Discussion Document.

The further intention is that delivery of these specific outcomes will in turn ensure the supply of appropriate financial products and services to customers and enhanced transparency and discipline in financial institutions, resulting in improved customer confidence. The final desired outcome is that customers' financial services needs are appropriately met through a sustainable industry.

### ***The six fairness outcomes***

The TCF fairness outcomes, positioned from the perspective of the customer, are the following:

- **Outcome 1:** Customers are confident that they are dealing with firms where the fair treatment of customers is central to the firm 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.<sup>4</sup>
- **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.

### ***Fairness outcomes to be delivered throughout the product life cycle***

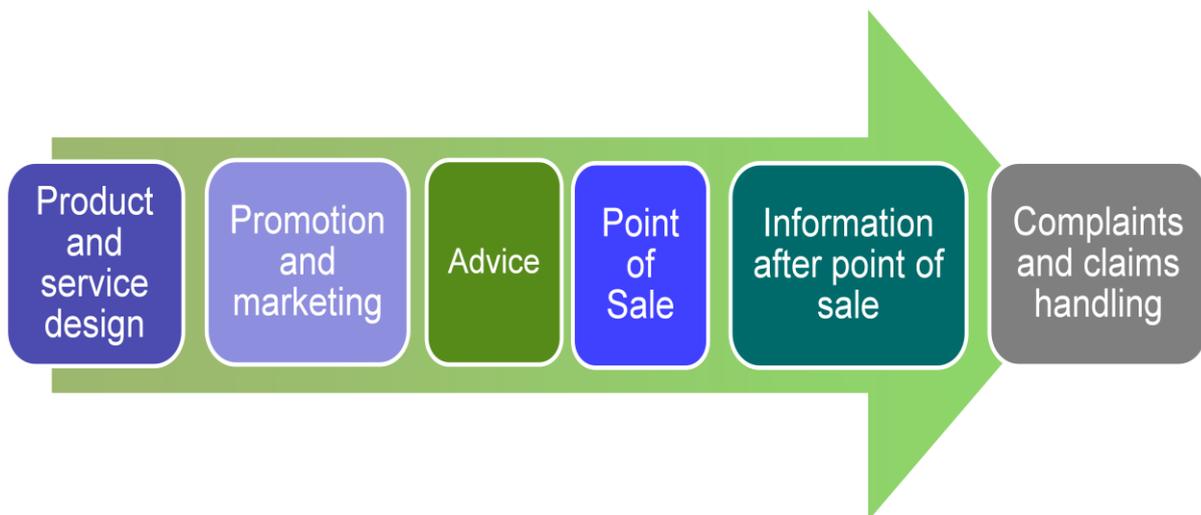
TCF will require regulated firms to consider their treatment of customers at all stages of their relationship with the customer, from product design and marketing, through to the advice, point-of-sale and after-sale stages. Firms will ultimately be required to demonstrate – through management behaviours and monitoring – that they are consistently treating customers fairly throughout the stages of the product life cycle to which they contribute.

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<sup>4</sup> The National Treasury has identified “expanding access through financial inclusion” as one of its financial sector policy priorities. Accordingly, firms operating in lower income target markets will be expected to give due regard to financial inclusion objectives in designing products, services and distribution strategies for these customer groups.

The 6 fairness outcomes can be applied to the stages of a typical product life cycle as shown in Figure 1.

**Figure 1: TCF and the product life cycle**



- **Product and service design:** Products and services – and the distribution strategies chosen to bring them to market – are designed and developed for specific target markets, based on a clear understanding of the likely needs and financial capability of each customer group.
- **Promotion and marketing:** Products are marketed to specific target groups, through clear and fair communications that are not misleading and are appropriate to the target group.
- **Advice:** Firms need to ensure that, where advice is provided, advisers are fully equipped to provide advice that is suitable to the needs of the customer concerned, balancing the commercial objective of increasing sales with the objectives of TCF and avoiding conflicts of interest.
- **Point-of-sale:** Firms need to provide clear and fair information to enable customers to make informed decisions about transacting with the firm, its products and services. This means that product risks, commitments, limitations and charges must be transparent. Disclosure around bundled products must enable customers to understand the different components of the bundle.
- **Information after point-of-sale:** Firms need to provide customers with ongoing relevant information to enable them to monitor whether the product or service continues to meet their needs and expectations, and provide acceptable levels of service for post-sale transactions or enquiries. Firms must also monitor and respond to changes in the wider environment that may affect products and impact on particular groups of customers.

- **Complaints and claims handling:** Firms need to honour representations, assurances and promises that lead to legitimate customer expectations. Legitimate expectations must not be frustrated by unreasonable post-sale barriers. There is a requirement for fair and consistent handling of claims and a mechanism to deal with complaints timeously and fairly. Firms should undertake to identify common underlying causes of complaints and take action to eliminate the root cause.

**Ultimate desired outcomes of TCF**

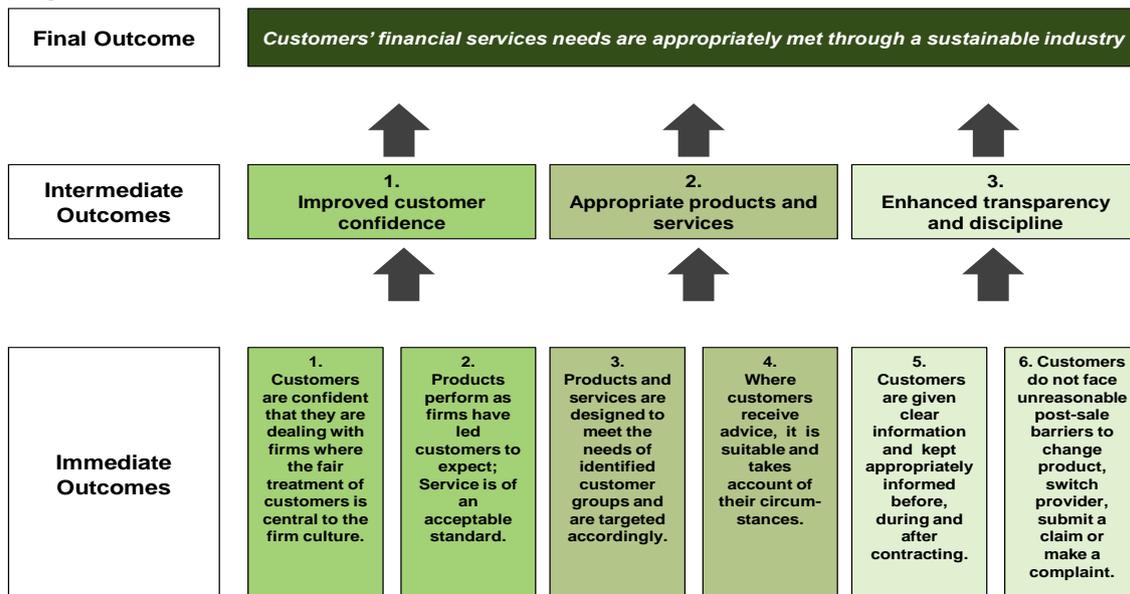
From the perspective of the customer, the FSB’s vision for the industry is a market conduct framework that will ensure that **customers’ financial services needs are appropriately met through a sustainable industry.**

The TCF programme is intended to contribute to this final, desired outcome for the sector, by delivering the following intermediate outcomes:

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

These intermediate outcomes can be mapped back to the six specific fairness outcomes as shown in Figure 2:

**Figure 2: Desired outcomes of TCF**



## TCF and the FSB's market conduct mandate

On 23 February 2011, the National Treasury published a policy document entitled “*A safer financial sector to serve South Africa better*” (*NT Policy Document*). In it, proposals to strengthen financial sector regulation, both in response to lessons learnt from the recent global financial crisis and in response to South Africa's own domestic financial sector challenges are set out.

One of the key policy priorities for financial sector regulation identified in the NT Policy Document is **consumer protection and market conduct**. Other key policy priorities are **financial stability, expanding access through financial inclusion** and **combating financial crime**. The NT Policy Document also stresses the importance of market conduct regulation's role in complementing prudential (financial soundness) regulation. Market conduct malpractices contributed palpably to sustainability and systemic risks in the recent global financial crisis.<sup>5</sup>

Given the policy priorities of strengthening both prudential and market conduct regulation, South Africa will move towards a “twin peaks” model of financial regulation – with one regulator tasked with prudential regulation of the sector, and another tasked with market conduct regulation. The South African Reserve Bank is seen as best placed to play the role of macro prudential regulator<sup>6</sup>, while the FSB will focus on market conduct regulation, with its mandate extended to include market conduct regulation of retail banking.

The “twin peaks” regulatory model will therefore mean “substantially stronger market conduct regulation at the FSB”<sup>7</sup>. The NT Policy Document highlights the TCF initiative as “an important step in strengthening market conduct objectives in the financial sector”. TCF is described as “a framework for tougher market conduct oversight” which it is hoped will lead to more optimal outcomes from the perspective of regulators, consumers and ultimately firms.<sup>8</sup>

The FSB has therefore been given an unequivocal mandate by the National Treasury to introduce TCF as a key mechanism to drive the policy priority of ensuring consumer protection through strengthened market conduct regulation. The FSB intends to use the TCF programme as the blueprint for its enhanced market conduct regulatory approach.

<sup>5</sup> See pp13 and 40 of the NT Policy Document.

<sup>6</sup> p31 of the NT Policy Document

<sup>7</sup> p46 of the NT Policy Document

<sup>8</sup> p42 of the NT Policy Document

## CHAPTER 3:

# A structural model to deliver TCF

Delivering TCF outcomes for retail financial services consumers will require action by both firms and the FSB. In addition, various supporting initiatives involving engagement with other stakeholders will need to be in place. The TCF model will consist of three main focus areas, or “pillars”, each of which will place specific obligations on firms and the FSB respectively. Each of the TCF pillars will be discussed in greater detail in the following chapters, but are summarised in Figure 3.

**Figure 3: Delivering TCF – a structural model.**

	<b>PILLAR 1: The TCF framework</b>	<b>PILLAR 2: Implementing TCF</b>	<b>PILLAR 3: Incentives &amp; deterrence</b>
<b>Firms</b>	<b>Regulatory framework</b> A regulatory framework will be developed, within which firms must conduct their business. The framework will comprise a combination of market conduct principles and explicit rules.	<b>Culture and governance</b> Firms must demonstrably embed a TCF culture, supported by controls, governance structures, management information and self-assessment.	<b>Disclosure and reporting</b> Firms will be required to publicly disclose identified TCF performance measures and submit non-public TCF reports as required by the FSB.
<b>Financial Services Board</b>	<b>Supervisory framework</b> The FSB will develop a framework for effective, intensive and intrusive supervision of firms' adherence to the market conduct regulatory framework. The framework will comprise appropriate monitoring, reporting, off-site analysis and on-site visit components.	<b>Proactive supervision</b> The FSB must implement the supervisory framework to enable proactive monitoring of and response to industry (macro) and firm-specific (micro) TCF risks and outcomes.	<b>Enforcement mechanisms</b> The FSB will enforce the TCF framework through a combination of pre-emptive intervention for identified industry and firm-specific conduct risks, regulatory sanctions (with “naming and shaming” ) for firms in breach, and prosecution of individual wrongdoers.
<b>Support structures</b>	<i>Ultimate fairness –</i> Ombuds with jurisdiction will ensure resolution of TCF failings for specific customers, and share information with the FSB to identify industry conduct risks.		
	<i>Regulatory co-ordination and information sharing</i> The FSB will take the lead on market conduct initiatives in the sector and co-ordinate with other market conduct regulators. Market conduct regulation will complement prudential regulation to maximise consumer protection under a “twin peaks” financial sector regulatory model.		
	<i>Consumer education and awareness –</i> TCF will be taken into account in FSB and national consumer education strategies.		

## CHAPTER 4:

# Pillar 1 - The TCF framework

### **Firms will conduct business within a TCF regulatory framework**

Although the implementation of TCF will be guided by the six broad fairness outcomes, clear, enforceable rules and regulations must also be in place to ensure that these outcomes are achieved. Experience has shown that relying on firms to “do the right thing” is not on its own sufficient to drive the behavioural and culture change required to deliver consistently fair outcomes for customers. Delivery of TCF therefore requires the development of a regulatory framework that will effectively balance principles-based and rules-based regulation to ensure that regulated firms deliver the desired outcomes of discipline and transparency in a consistent manner.

The regulatory framework will consist of an appropriate mix of legislation, subordinate legislation and specific guidance for firms, to ensure that firms clearly understand the FSB’s regulatory expectations. Firms will be required to develop processes and controls to manage their compliance with the rules-based components of TCF. Although it is important to stress that firms should not treat their TCF delivery strategy as a “compliance project”, to the extent that TCF will require compliance with specific rules, the compliance and risk management functions within firms will need to form part of the firms’ overall TCF strategy. Ultimately, achievement of the TCF outcomes will be the responsibility of the firm’s management and board.

#### ***Aims of the regulatory framework***

The TCF regulatory framework will aim to achieve:

- *Consistency.* The framework must be developed to deliver consistently fair outcomes for customers across the retail financial sectors the FSB regulates<sup>9</sup>. It will be necessary to ensure that similar rules are applied to categories of firms, products and services that entail similar levels of market conduct risk. The framework must minimise opportunities for regulatory arbitrage between different parts of the financial sector.<sup>10</sup>

<sup>9</sup> In the initial phases of implementation, the FSB’s TCF mandate will not yet cover the retail banking sector, other than to the extent that its financial intermediation activities are already subject to the FAIS Act. In view of the proposed extension of the FSB’s market conduct jurisdiction to cover the banking sector, it is however expected that banks will in time fall under the broader TCF umbrella as the “twin peaks” regulatory model is finalised.

<sup>10</sup> The NT Policy Document (p.26) stipulates one of the Principles behind reforming the financial regulatory systems as: “Regulations should be of universal applicability and comprehensive in scope in order to reduce regulatory arbitrage.”

- *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:* Chapter 3 of the NT Policy Document sets out various principles behind reforming the financial regulatory system. One of these is that the other principles are reflected in international standards like Basel III and standards set by the International Association of Insurance Supervisors (IAIS) and the International Organisation of Securities Commissions (IOSCO). The NT Policy Document goes on to state that “to the extent that there are any contradictions or inconsistencies in the above principles (i.e. the NT principles), the international standards will apply.” Our policymaker’s commitment to international regulatory best practice is therefore clear.<sup>11</sup>

### ***Stakeholder engagement***

The FSB will engage with affected stakeholders from the financial services industry, ombud schemes, consumer and regulatory experts and other market conduct regulatory authorities to obtain input and support in developing the TCF regulatory framework. This is dealt with in greater detail in Chapter 8.

### ***Regulatory themes***

The TCF regulatory framework will focus on a number of regulatory themes, aligned to the six TCF fairness outcomes set out in Chapter 2. Existing regulation within each of these themes will be reviewed for adequacy in delivering the TCF outcomes. The types of regulation mentioned below that will be reviewed under each theme are illustrative and not exhaustive. These themes are:

- **Outcome 1 - TCF culture:** Regulation dealing with how TCF outcomes are dealt with within the governance structures of firms, such as fit and proper requirements for management, audit, risk and compliance requirements, board and committee structures, whistleblower protection rules, management incentives.
- **Outcome 2 - Appropriately targeted design and marketing of products and services:** Regulation dealing with product features, charging structures, product governance and approval processes, unfair terms, undesirable business practices, regimes for particular consumers such as products aimed at addressing inclusion; and marketing and advertising restrictions and standards.
- **Outcome 3 - Clear information:** Regulation dealing with specific disclosure obligations, disclosure standards, plain language, language policies, electronic and telephonic communications, misleading representations.

<sup>11</sup> p.27 of the NT Policy Document

- **Outcome 4 - Suitable advice:** Regulation dealing with financial advisory obligations (primarily under FAIS), distribution models, legal relationships between intermediaries and product suppliers, conflicts of interest (under FAIS and more broadly), adviser remuneration.
- **Outcome 5 - Products perform as expected and acceptable service:** Regulation dealing with product and performance monitoring, ongoing communication, reasonable benefit expectations, service levels, operational ability and capacity, outsourced suppliers, business continuity, record keeping, information security, fraud risk management, succession planning.
- **Outcome 6 - No unreasonable post sale barriers:** Regulation dealing with access to information, complaints handling, claims handling, alternative dispute resolution, product flexibility, product portability, termination charges.

### ***Scope of the regulatory framework***

It will be necessary to clearly define which categories of financial products and services are regarded as having a “retail” impact for purposes of TCF, and therefore which firms will be obliged to deliver some or all of the TCF outcomes.

Relevant considerations, where stakeholder views will help to inform the regulatory framework, include:

- **Whether it will be necessary to define the term “retail”, “retail customer” or “retail product or service” for TCF purposes?** TCF is intended to protect ordinary financial consumers who would typically be vulnerable to unfair treatment as a result of having unfair bargaining power and asymmetrical access to information, as compared to financial firms. As such, it is not limited only to protection of natural persons and should also ensure fair treatment of juristic entities that also have these vulnerabilities. However, given that the South African regulatory framework does not recognise a general concept of “sophisticated” or “professional” clients, who require less rigorous consumer protection, it should be debated whether an intuitive approach to defining “retail” customers will suffice in understanding where to draw this line. On the other hand, an explicit definition creates the risk of firms relying on definitional “loopholes” to avoid TCF responsibility.<sup>12</sup>
- **To what extent will “wholesalers” be brought within the scope of TCF?** The primary focus of TCF will be on those firms that manufacture products or provide services (including advice and intermediary services) directly to retail customers. Where manufacturers of such retail products are concerned, it will not make a difference that they use intermediaries to distribute their products - clearly in such a case both the product manufacturer and the intermediary will be required to ensure fair treatment of their shared customers. Further discussion and guidance will be required in those cases where there are various firms in the overall “value chain” that ultimately results in a retail financial product or service being provided to a customer. For example, consider the scenario where an investment bank designs an over-the-counter derivative structure, on-sells it to a collective investment scheme management company who incorporates it into a CIS, and the CIS then enters into

<sup>12</sup> The FSA in the UK has not seen the need to define “retail” in the TCF context, although they do classify clients as “retail”, “professional” etc. for other regulatory purposes.

agreements with both long-term insurers and administrative financial services providers (commonly referred to as linked investment service providers or “LISP’s”) to offer exposure to the CIS scheme – incorporating *inter alia* the original OTC structure – to their retail customers by “wrapping” it in their retail offerings. These retail offerings are in turn recommended to the retail customer by an independent financial adviser. In this case, how much (if any) accountability for fair treatment of the end retail customer should be borne by the investment bank, the CIS management company, the long-term insurer, the LISP, and the financial adviser respectively? A sensible approach will be required to balance what can reasonably be expected from the firm in question given the extent of its ability to foresee and influence the customer outcome, against the fact that firms should not be able to shirk TCF accountability purely because they do not have any direct interaction or contractual relationship with the retail customer.<sup>13</sup>

- What will the impact of TCF be on financial intermediaries, given their existing FAIS obligations?** Clearly the FAIS Act already imposes extensive obligations on authorised financial services providers and their representatives that are relevant to the TCF fairness outcomes. In particular, intermediaries’ delivery of fairness outcomes 3 (clear information) and 4 (suitable advice) are to a large extent driven by the disclosure, advice, conflict of interest and licensing requirements under the FAIS Act. However, it does not follow that TCF will have no additional impact on FAIS regulated intermediaries. Where the FAIS obligations are largely compliance and rules based, the outcomes based TCF framework will require intermediaries to ensure that their adherence to FAIS is complemented by being able to demonstrate that they have embedded the broader TCF culture framework within their organisations (TCF fairness outcome 1). From a risk-based perspective, the culture and governance dimensions will require particular attention by larger financial services providers. Intermediaries will however also be expected to consider their role in delivering TCF fairness outcomes 2, 5 and 6 (the outcomes related to appropriate product and service design, product performance and service levels, and post-sale barriers). Although the primary responsibility for these outcomes will rest on product suppliers themselves, financial intermediaries can and should bring greater pressure to bear on product suppliers to ensure that inappropriately designed and marketed products, poor post-sale service practices, and unreasonable post-sale barriers are challenged. A useful distinction can be drawn between ensuring a product is **appropriate** for a particular target market, and ensuring the product is **suitable** for the particular customer concerned. The former is mainly the product supplier’s responsibility, and the latter is mainly the intermediary’s responsibility. However, it does not follow for example, that an intermediary can abdicate responsibility for recommending an unfairly or inappropriately structured product to a customer on the basis that ensuring fair product design is the product supplier’s responsibility. An appropriate level of product “due diligence” is expected from intermediaries. Conversely, product suppliers cannot disregard poor selling practices of their products by intermediaries, for example where they are aware that products from their range are being sold to the wrong customers, and argue that it is solely the intermediary’s responsibility to ensure the product is suitable to the customer who

<sup>13</sup> See the FSA’s Policy Statement PS07/11, “Responsibilities of providers and distributors for the fair treatment of customers”, published in July 2007, as an example of the type of guidance that may be provided in this regard. The FSA Policy Statement is available at [www.fsa.gov.uk/pubs/policy](http://www.fsa.gov.uk/pubs/policy).

purchases it. TCF will require product suppliers and intermediaries to share accountability for fair treatment of their mutual customers.

- How will TCF be applied to retirement funds?** Retirement funds are a particular example of where the debates regarding what is “retail” business and how “wholesalers” should be treated, can arise. This is due to the complex set of legal relationships that exist between retirement funds, their trustees, their benefit administrators, their investment administrators, their insurers (for underwritten funds), their advisers and other service providers, their sponsors or participating employers (where applicable) and, ultimately, their members. It seems clear that retirement annuity funds, pension preservation funds and provident preservation funds, where fund members enter into individual membership contracts - typically underpinned by individual insurance or collective investment scheme products - must be regarded as retail business for TCF purposes. However, even in these cases, further work will be required to identify the TCF accountabilities of the various role-players in the value chain.<sup>14</sup> Arguably, commercially operated umbrella retirement funds, particularly where participating employers are primarily small to medium sized businesses, should also be regarded as retail operations for TCF purposes. Again, however, an assessment of TCF accountabilities will be required.
- How will TCF be applied to financial services rendered under the supervision of the JSE and STRATE?** Financial services provided by authorised users (stockbrokers) and other regulated persons in terms of the Securities Services Act, 34 of 2006<sup>15</sup>, are currently exempt from the provisions of the FAIS Act<sup>16</sup>, and are instead subject to the conduct rules imposed by statutorily recognised self-regulatory organisations (the JSE and STRATE). A number of these entities do however provide advice and other financial services to retail customers. The question therefore arises as to how the delivery of TCF outcomes should best be ensured for these customers within the regulatory framework. In line with the risk-based approach of the TCF framework, the FSB will engage with the self-regulatory organisations to determine the extent of any conduct risks and assess whether any additional consumer protection measures are warranted.

### ***Regulatory alignment analysis***

Once the regulatory themes described above have been more fully described, an analysis of existing legislation, subordinate legislation and, where applicable, codes of conduct will be undertaken, to identify gaps and inconsistencies (a) between the various existing provisions themselves in relation to TCF related matters and (b) between the existing provisions and their likely effectiveness in delivering the TCF fairness outcomes. The regulatory alignment analysis will be broken down into the regulatory themes. The analysis will be required in respect of both legislation supervised by the FSB as well as legislation supervised by other

<sup>14</sup> This differs from the situation in the United Kingdom, where individual retirement products are typically purely contractual arrangements between product suppliers and consumers, and are not always included in a “trust” or “fund” type arrangement, making the application of TCF principles simpler.

<sup>15</sup> Due to be repealed and replaced by the proposed Financial Markets Act, once promulgated.

<sup>16</sup> Exemption from FAIS applies to the extent that the relevant activities are already regulated.

government departments and regulatory agencies, to the extent that it is relevant to the achievement of TCF outcomes.

FSB supervised legislation to be analysed is:

- Collective Investment Schemes Control Act, 45 of 2002
- Financial Advisory and Intermediary Services Act, 37 of 2002
- Financial Institutions (Protection of Funds) Act, 28 of 2001
- Financial Services Board Act, 97 of 1990
- Financial Services Ombud Schemes Act, 37 of 2004
- Financial Supervision of the Road Accidents Fund Act, 8 of 1993
- Friendly Societies Act, 25 of 1956
- Inspection of Financial Institutions Act, 80 of 1998
- Long-term Insurance Act, 52 of 1998
- Pension Funds Act, 24 of 1956
- Securities Services Act, 36 of 2004<sup>17</sup>
- Short-term Insurance Act, 53 of 1998
- Subordinate legislation under the above Acts.

Other potentially relevant legislation includes (but is not necessarily limited to):

- Consumer Protection Act, 68 of 2008<sup>18</sup>
- National Credit Act, 34 of 2005
- Banks Act, 94 of 1990
- Protection of Personal Information Act (currently still a Bill)
- Companies Act, 71 of 2008
- Competition Act, 89 of 1998
- Financial Intelligence Centre Act, 38 of 2001
- Income Tax Act, 58 of 1962
- Medical Schemes Act, 31 of 1998
- Promotion of Equality and Prevention of Unfair Discrimination Act, 4 of 2000
- Constitution of the Republic of South Africa, 1996
- Relevant subordinate legislation under the above Acts.

Consideration will also be given to the role that industry association conduct standards can play in reinforcing the delivery of TCF outcomes by their member firms. Any decisions in this regard will be informed by relevant competition considerations and an analysis of the likely effectiveness of self-regulation in the particular context.

<sup>17</sup> Due to be repealed and replaced by the proposed Financial Markets Act, once promulgated

<sup>18</sup> The principles set out in the Consumer Protection Act will, wherever relevant, be a key input into developing the TCF regulatory framework. However, as noted in the NT Policy Document, it must be stressed that financial services in fact require higher “standards of conduct that are more stringent than those generally applied to other non-financial goods and services” in view of the particular risks they pose. The Consumer Protection Act principles will therefore serve as at least a minimum standard of consumer protection. (See pp.41 and 42 of the NT Policy Document.)

**Legislative recommendations**

On completion of the regulatory alignment analysis, a set of regulatory amendment recommendations will be developed for each of the regulatory themes. Additional regulatory recommendations may be made to address the FSB's enforcement and supervision powers, if the supervisory framework analysis discussed later in this chapter identifies a need to strengthen them. Together, these recommendations will comprise the FSB's proposed TCF regulatory framework.

**Regulatory co-ordination**

The NT Policy Document stresses the importance of co-ordination between regulators as a key feature of the financial regulatory framework and proposes the creation of a Council of Financial Regulators to provide "interagency co-ordination between regulators on issues of legislation, enforcement and market conduct."<sup>19</sup> As mentioned above, and discussed further in Chapter 8, stakeholder engagement in developing the regulatory framework will include engagement with other relevant market conduct regulators. In addition, although the processes of the Council of Financial Regulators are still to be developed, it is probable that formal engagement on the proposed TCF regulatory framework with this Council or mandated sub-structures of the Council will need to take place.

**Finalising the regulatory framework**

Once the various stakeholder engagement and consultation processes described above have been concluded, the final regulatory proposals will be subject to the normal legal processes for finalising the legislation and subordinate legislation concerned. This includes full public consultation and Parliamentary deliberation processes where required.

**The FSB will develop a TCF supervisory framework**

Supervision of the outcomes based TCF regulatory framework, with its combination of rules based and principles based regulation, will require an appropriate supervisory framework.

**Aims of the supervisory framework**

An effective TCF supervisory framework must be:

- *Risk-based and proportional:* In line with the FSB's existing risk-based supervisory approach, 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.<sup>20</sup>
- *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:* To enable the FSB to carry out proactive and pre-emptive supervision, particularly at the level of individual firms, oversight will need to be more intensive and intrusive than has been the case historically – albeit in a risk-based manner.

<sup>19</sup> p.5 of the NT Policy Document. Also see p.35.

<sup>20</sup> The NT Policy Document (p.43) states that "regulatory proposals will be subject to an assessment to ensure that they are in proportion to the nature, scale and complexity of the market conduct risks that are present in different industries and business models."

***Enhanced supervisory techniques and capacity***

The TCF supervisory framework will require the FSB to enhance its traditional supervisory techniques. 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. Enhanced supervisory techniques required to implement TCF are discussed in further detail in Chapter 5. An analysis of the FSB's skills and capacity to apply the enhanced supervisory approach will be undertaken, and necessary additional capability will be built. Targeted training on specific products and business models and the conduct risks they present will form part of this capacity building process.

## 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**. If such a culture is truly embedded in the firm's "DNA", delivery of the remaining five fairness outcomes should follow as a matter of course. Conversely, if there is no true commitment to embedding a TCF culture, firms will struggle to meet the remaining fairness outcomes consistently.

#### *Embedding a TCF culture*

In order to fully embed a TCF culture, firms will need to focus on TCF outcomes at all stages of the product life cycle to which they contribute (as discussed in Chapter 2) and also at all levels of planning, decision making, management and operations within the firm.

Firms that choose to ring-fence TCF responsibilities within specific organisational functions, such as the compliance or risk management functions, or task only specific staff members, such as one or more "TCF champions" or customer service managers with delivering TCF, are unlikely to successfully achieve the TCF outcomes.

Although there will be elements of the TCF regulatory framework that will require compliance with specific rules, implementing TCF should not be regarded as a compliance implementation project. 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*

To ensure the behaviours and attitudes necessary for TCF, firms will be expected to build a TCF approach into the following organisational structures and processes:

- **Leadership:** The Board, senior and middle management need to provide direction and monitor the delivery of TCF behaviours and outcomes. TCF must be "owned" by the most senior management structures within the organisation, which will be held to account to ensure the delivery of TCF outcomes at all levels. The importance of TCF must not only be understood, it must also be implemented in all business areas and this requires meaningful "top down" direction.
- **Strategy:** The TCF aims should not merely be part of a firm's stated vision and values. They also need to be carried through to implementation as part of the firm's broader business strategy. The TCF approach should be built into any strategic and business plans (or changes in plans) developed by senior management and should form an essential component of any strategic planning processes.

- **Decision-making:** Decision-making protocols should ensure that decisions are tested for customer impact. All decisions that impact on customers should be subject to the challenge implicit in the TCF strategy of the company. For staff to feel they can evaluate and challenge decisions from the TCF perspective - without repercussion - it may be necessary to set processes in place or to create a conducive environment.
- **Governance and controls:** The governance structures and control mechanisms within firms will need to be designed to create disciplines around TCF. For example, governance processes around product approval, distribution models, service standard setting, claims reviews and complaint escalations would all need to cater for TCF considerations. It will also be necessary to develop appropriate management information and measurement systems to ensure that the success of a firm's TCF strategy can be measured and that TCF risks can be identified. Governance and control mechanisms will also need to be in place to ensure the firm's compliance with the explicit rules-based components of the TCF regulatory framework and to deliver any reports that may be required by the FSB.
- **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. This should not apply only at the level of customer-facing staff, but also at middle and senior management levels to ensure that both staff and management are appropriately held to account for TCF successes and failures.
- **Reward:** Remuneration, incentive and reward policies need to take cognisance of fair customer outcomes and entail consequences for TCF successes and failures. Incentivising other essential business goals such as profit and sales volumes must be reasonably balanced against encouraging TCF. Reward practices may therefore need to be reviewed to ensure that conflicts of interest are avoided and unreasonable risk-taking at the expense of customer protection is not incentivised.

The FSB will issue specific guidance from time to time regarding its expectations of firms in embedding the TCF culture framework.

### ***Measurement and management information***

For the TCF initiative to be successful, firms must be in a position to provide objective evidence that they are treating their customers fairly and have embedded TCF in their organisational culture. This will require management information (MI) mechanisms designed to **monitor** and **measure** the firm's performance in delivering the six fairness outcomes and the elements of the TCF culture framework set out above. A combination of qualitative and quantitative MI will probably be needed. Firms will also be expected not only to have effective MI in place, but also to show that they have analysed the MI they have gathered to identify TCF risks and areas for improvement and **acted upon** these findings to enhance their customers' experience.

In addition to having MI in respect of their "business as usual" practices, firms should also have mechanisms in place to monitor and respond to changes in the broader environment – such as economic and regulatory developments – that could impact on customers and their financial needs. This will enable firms to pro-actively identify conduct risks and pre-empt possible unfair outcomes, or at least to respond promptly where adverse customer impacts arise.

### ***Self assessment***

Irrespective of any specific regulatory TCF reporting requirements that may be prescribed, firms will be expected to use their MI mechanisms to assess their own success rates in delivering TCF outcomes. They will also be expected to use the findings of their self-assessments to set firm-specific TCF goals and raise their TCF standards where areas for improvement are identified. Although the FSB will develop a self-assessment tool and associated guidance, which firms can use for this purpose, firms will be well advised to develop their own self-assessment tools that are appropriately tailored to their own business models.<sup>21</sup>

### **An enhanced supervisory approach by the FSB**

The FSB's supervisory approach must be broadened to pro-actively identify potential areas of concern or stress, with a greater emphasis on pre-empting negative consumer outcomes where possible, rather than reacting to complaints or already crystallised prejudice. This proactive approach will need to cover both emerging risks within specific firms (micro conduct risks), as well as concerns at an industry, sector or business model level (macro conduct risks).<sup>22</sup>

To enable it to make fair and informed judgements regarding unacceptable TCF risks within a firm, the FSB will need to have clear insight into the extent to which TCF has been embedded in the firm's culture. This will in turn require more intensive supervision and more comprehensive reporting by firms. Once risks have been identified, intrusive engagement with the firm will be required to try to rectify the situation and pre-empt consumer harm – or seek redress where harm has occurred.

### ***Reporting requirements***

These will need to be sufficiently comprehensive and rigorous to put the FSB in a position to pro-actively identify industry level (macro) and firm-specific (micro) conduct risks and early warning signs of unfair customer treatment. An appropriate range of reporting mechanisms will be developed, in consultation with industry and other stakeholders, as part of the supervisory framework.

These reporting mechanisms will include both non-public components, to be incorporated as appropriate into existing regulatory returns and / or compliance reports, as well as public disclosure of identified TCF related measures. This is discussed further in Chapter 6.

### ***On-site supervision***

On-site supervision will include both specific examination and assessment of a firm's TCF related processes and management information, as well as engagement with board members (including non-executives) and senior and executive management, to form a view of the extent of leadership commitment to a TCF culture.

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<sup>21</sup> See Chapter 8 for further detail on the self-assessment tool to be developed by the FSB.

<sup>22</sup> For an illustrative example of regulatory monitoring of macro conduct risk, see the FSA's "Retail Conduct Risk Outlook, 2011", available at [www.fsa.gov.uk/pubs/other](http://www.fsa.gov.uk/pubs/other).

## ***Off-site supervision***

Off-site supervision can include – in addition to the traditional off-site evaluation of the firm’s regulatory returns - measures such as “mystery shopping” interactions with firms and intermediaries, and surveys of customers and intermediaries, to test customer experience “on the ground”. Inputs from other stakeholders such as ombud schemes, other regulators, consumer organisations and the media will also be considered.

## 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. A TCF programme has to do more than rely on the industry to do the “right thing”. A viable TCF approach requires credible deterrence measures. Credible deterrence means that market participants must know that unfair treatment of customers will be detected and that those responsible for unfair treatment will face consequences. They must also appreciate that fair treatment of customers will be to their advantage.

The approach to incentives and deterrence will require firms to be able to provide clear information on their TCF performance, and require the FSB to analyse and respond effectively and decisively to this information.

### **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. As discussed in Chapter 5, this will *inter alia* entail comprehensive and rigorous disclosure and reporting requirements. Both public and non-public reporting is envisaged.

#### ***Public disclosure of identified TCF performance measures***

Possible items which firms will be required to disclose publicly could include measures relating to claims statistics (e.g. repudiations, disputes, timelines), complaints volumes and responses, adherence to service levels, investment performance against benchmarks, and regulatory sanctions or interventions. Public disclosure is likely to apply both in respect of specific firms’ measures and also on an aggregated basis, where appropriate, at industry or sector level. Effective aggregation processes will be required.

Care will have to be taken to ensure that public disclosure leads to fair and meaningful comparisons between firms and sectors – that “apples are compared with apples”. The reputational impact of meaningful public disclosure can then act as a powerful deterrent of unfair customer treatment, and an incentive for firms to compete over the quality of the customer experiences they deliver. TCF reporting information per sector can also encourage firms to apply peer pressure to competitors that are not delivering adequate TCF outcomes. It may be that publication of such information may lead competitors to report negative behaviour to the relevant authorities, to avoid the sector’s reputation being tainted by the conduct of “bad apples”.

Conversely, those firms who perform well on publicly disclosed TCF measures should gain competitive advantage from improved public and stakeholder perceptions. Although arguably this should in itself constitute a sufficient positive incentive (“carrot” as opposed to “stick”) for adhering to TCF principles, the FSB may consider additional methods of reinforcing positive TCF outcomes. In a risk-based supervisory framework, firms who consistently and

demonstrably deliver on their TCF commitments will also attract proportionally less regulatory scrutiny than their riskier competitors.

Through correctly structured public reporting, a measure of market discipline will therefore come to bear on firms that will incentivise TCF delivery. Although this will not preclude further regulatory action where warranted, it may in specific cases support the pre-emptive aims of the TCF approach by driving behaviour change in time to make regulatory intervention unnecessary or less severe.

### ***Non-public reporting as required by the FSB***

Over and above any publicly reported TCF measures, the FSB will require further, more granular, reporting on firm-specific TCF measures and practices. These will be incorporated appropriately into other ongoing regulatory returns and reports. In addition to such standard, regular reporting requirements, the FSB may also use its information access powers to request additional TCF related information where it deems this necessary – whether as part of scheduled risk-based supervision or in response to a particular concern.

Given the FSB's reliance on the quality of firms' reported information to conduct reliable risk-based supervision, misleading or poor quality reporting must attract severe consequences.<sup>23</sup>

## **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 – and will - enforce firms' TCF accountabilities. Consumers and other stakeholders must also have confidence in the regulator's enforcement powers. The FSB must not only develop the TCF framework and monitor its delivery, it must also enforce adherence to the framework. An analogy from road behaviour is applicable: It is not enough that traffic authorities prescribe speed limits and supervise road behaviour (via speed traps, for example) – they also need to ensure that those caught exceeding the speed limits are punished in a way that discourages similar behaviour in the future.

### ***Pre-emptive intervention for industry conduct risks***

Chapter 5 has explained that the FSB's supervisory approach will be broadened to proactively identify emerging conduct risks, with a view to pre-empting negative consumer outcomes. This proactive approach will need to cover both risks within specific firms (micro conduct risks), as well as concerns at an industry, sector or business model level (macro conduct risks). Where such risks are identified, the FSB will need to take action to mitigate these risks to prevent or minimise harm to consumers. Where macro industry- or sector-wide risks are concerned, the regulatory response will need to be appropriate to ensure consistent, sector-wide behaviour change.

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<sup>23</sup> See NT Policy Document, p.25.

Possible types of intervention include:

- Engagement with appropriate industry associations to drive sector-wide communication and, where it is likely to be effective<sup>24</sup>, self-regulation through industry standards or codes of conduct.
- Issuing specific guidance to alert affected sectors of the FSB's concerns and expectations in regard to the risk identified.
- Thematic on-site monitoring of relevant firms to gain more comprehensive information of the extent of the risk (or breach, where applicable) concerned.
- Publishing warnings or other guidance to consumers of the financial products or services concerned.
- Introducing new regulations or tightening existing regulations (subordinate legislation).
- Proposing legislative changes after due consultation.

A particular question that will require debate is the matter of **whether or to what extent the regulator should intervene in the actual structure of financial products**, where products or product features are identified as being unfair to consumers – or at least to certain categories of consumers<sup>25</sup>. A range of possible interventions exists, with different international examples. These range from regulatory pre-approval of financial products before launch, the most interventionist extreme, to mere compulsory disclosure of key product features, the least interventionist extreme. A number of other options exist inbetween, including prescription of certain product features for certain target markets and powers to “ban” or order withdrawal of certain products or product features.<sup>26</sup> Future decisions around product intervention levels will need to be an outcome of the micro and macro market conduct risk assessment processes described in this chapter, and the regulatory alignment analysis described in Chapter 4.

### ***Pre-emptive intervention for firm-specific conduct risks***

In addition to the identification of industry (macro) conduct risks discussed above, Chapter 5 also dealt with the need to proactively identify conduct risks in specific firms, through more intensive supervision. Again, where such risks are identified, the FSB will need to take action to mitigate these risks to prevent or minimise harm to consumers.

<sup>24</sup> The NT Policy Document (p.13) makes the point that “the idea that the financial sector can successfully regulate itself has lost credibility in the aftermath of the crisis.” Nevertheless, it is possible that in appropriate cases a measure of self-regulation can serve to complement intensive and pre-emptive regulatory supervision.

<sup>25</sup> The NT Policy Document (Chapter 4) highlights “high and opaque fees” of financial products as a specific policy concern, and identifies particular product related market conduct concerns in various sectors. These include certain transactional fees in the retail banking sector; early termination charges, up front remuneration practices and conflicts of interest in the long-term insurance sector; high costs, conflicts of interest and aspects of consumer credit insurance in the short-term insurance sector.

<sup>26</sup> See the FSA’s Discussion Paper DP11/1 on “Product Intervention”, published on 25 January 2011, for a discussion of the range of possible product interventions being considered by the FSA in the UK. The Discussion Paper is available at [www.fsa.gov.uk/pubs/discussion](http://www.fsa.gov.uk/pubs/discussion).

Unless the FSB believes the risk is sufficiently serious to require immediate formal regulatory action, the FSB's likely initial response will be to **engage with the senior management concerned to reach agreement** on one or more of the following, as applicable:

- A course of action to ensure that the identified unfair treatment stops. This could include changes in business processes, or changes in product design or withdrawal of products or promotional material.
- Redress for customer prejudice already caused. This could include tracing and communicating with affected or potentially affected customers.
- Disciplinary or other appropriate action to be taken by the firm against those responsible for unfair treatment.
- Training interventions.

Where any such agreement is reached with a firm, explicit undertakings and timelines will be required and adherence to them will be closely monitored.

Where any such agreement is not honoured by the firm concerned, or where the FSB considers that the risk to consumers is so serious, or the conduct concerned is so unacceptable, that an agreed negotiated solution will not be effective or appropriate, formal regulatory enforcement action will be taken.

### ***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. A number of the following enforcement actions are already within the FSB's (or the applicable Registrar's) powers, or within the powers of the FSB **Enforcement Committee**.<sup>27</sup> However, the regulatory framework development described in Chapter 4 will include recommendations to enhance the FSB's enforcement powers where gaps are identified.

Enforcement options include:

- Administrative fines and penalties.
- Declaration of business practices to be undesirable, with associated powers to order cessation or amendment of the practices concerned.
- Suspension or withdrawal of regulatory licenses.
- Termination or withdrawal of the approval of certain individuals to act in certain capacities.<sup>28</sup>
- Damages and compensation awards (including punitive damages).
- Referral of certain matters to the High Court.
- Referral to the National Prosecuting Authority for criminal prosecution of individual wrongdoers, where a statutory or common law criminal offence is committed.

<sup>27</sup>As established by the Financial Services Board Act, 97 of 1990.

<sup>28</sup>Examples include but are not limited to removal of directors or withdrawal of licenses and debarment of representatives under the FAIS Act.

***“Name and shame”***

As discussed above, 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.

The legislation governing the powers of the FSB Enforcement Committee<sup>29</sup> already stipulates that any matters referred to the Committee – including cases where a settlement is reached between the parties and recorded as a determination of the Committee – are to be publicised. Publication is also prescribed for various other formal enforcement actions, such as withdrawal and suspension of licenses. Criminal proceedings, where applicable, are also a matter of public record.

In addition, the FSB will also consider a “name and shame” approach to less formal regulatory interventions. For example, the fact that an agreement has been entered into between the FSB and a firm to address identified conduct concerns, as described above, may or may not be made public by the FSB. This decision will be driven in the main by what the FSB considers to be in the best interests of affected or potentially affected consumers. Where the ability to publish such information would require strengthening of the FSB’s existing publication powers, legislative amendments will be considered in the course of developing the TCF regulatory framework.

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<sup>29</sup> Financial Institutions (Protection of Funds) Act, 28 of 2001 – see in particular s6G.

# CHAPTER 7:

## Support structures

Chapters 4, 5 and 6 have described 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. These pillars 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

Even the most comprehensive and rigorous of regulatory frameworks cannot guarantee that instances of abuse will never occur. Inevitably, some customers will be treated unfairly. It is therefore essential that such customers have ready access to simple and effective alternative dispute resolution mechanisms. In this way, they can be assured of “ultimate fairness”, even where the broader TCF framework has failed them.

In the financial sector, such mechanisms are provided by the various statutory and recognised voluntary ombud schemes contemplated in the Financial Services Ombud Schemes (FSOS) Act, 37 of 2004. Current schemes contemplated in the FSOS Act are:

- The Pension Funds Adjudicator.
- The Ombud for Financial Services Providers (commonly referred to as the FAIS Ombud).
- The ombuds of “recognised schemes”. These in turn refer to voluntary schemes that have been recognised in terms of s11 of the FSOS Act, and currently comprise the Long-term Insurance Ombudsman, the Ombudsman for Short-term Insurance, the Credit Ombud, the Ombudsman for Banking Services and the JSE Complaints and Disputes Scheme.
- The “statutory ombud”, created by the FSOS Act itself, who has jurisdiction in respect of complaints against financial institutions that do not fall within the jurisdiction of any of the above-mentioned ombuds. Accordingly, the FSOS statutory ombud has a “catch-all” jurisdiction in respect of complaints against financial institutions.

In their dealings with individual customer complaints, these ombud schemes are ideally positioned to provide the FSB with examples of emerging negative conduct trends and examples of specific unfair business practices. A number of the existing schemes have been helpful in providing the FSB with some of the examples of unbecoming conduct set out in the TCF Discussion Document. Going forward, the ombud schemes will play an important

role in supporting the FSB's aim to carry out pre-emptive supervision – both at macro (industry) and micro (firm-specific) level.

Equally, the ombud schemes will need to keep abreast of the proactive monitoring findings of the FSB, and the developing TCF regulatory framework, to assist them in recognising examples of abusive practices or TCF breaches in the cases referred to them. Individual matters dealt with by the ombud schemes will also provide valuable insight into the effectiveness of the TCF regulatory framework as it unfolds, and help to identify gaps in the framework.

Ongoing information sharing between the FSB and the ombud schemes will therefore make a vital contribution to all three of the TCF pillars: Designing the TCF regulatory framework, implementing TCF, and enforcing TCF.

## Regulatory co-ordination and information sharing

One of the main proposals set out in the NT Policy Document for strengthening the financial services regulatory framework is the need to promote greater co-ordination and information sharing between all financial regulators and establish a Council of Financial Regulators.<sup>30</sup>

A number of South African financial institutions, particularly financial conglomerates offering a range of financial products and services, hold a number of regulatory licences and fall under the jurisdiction of multiple financial regulators. A lack of co-ordination between these regulators therefore creates the risk of regulatory inconsistency and arbitrage, and even systemic risk.

Although the proposed move to a “twin peaks” regulatory model will help to ensure consistent regulatory focus on prudential and market conduct risks respectively, regulatory co-ordination and information sharing remains crucial for the following reasons:

- To ensure that **market conduct regulation and prudential regulation will complement each other in providing a holistically safer financial services sector**. The NT Policy Document stresses the importance of market conduct regulation's role in complementing prudential regulation, providing examples from the global financial crisis of where market conduct malpractices have been at the root of soundness and stability failures. Market conduct regulators will therefore need to be sufficiently aware of prudential regulatory policy and risks to be able to identify and communicate possible prudential or systemic impacts of market conduct malpractices. Similarly, prudential regulators must be in a position to recognise and communicate conduct risks arising from financial soundness concerns.
- To ensure that **the market conduct regulatory framework itself – of which the TCF framework is a key component – achieves its aims of consistency, completeness and co-ordination** outlined in Chapter 4.

Although the proposed Council of Regulators is likely to be the primary governance structure for formal inter-regulator co-ordination and information sharing, more frequent interactions with various market conduct regulators – both formal and informal – will be necessary. To achieve the further regulatory aim of complying with international best practice (see Chapter 4), liaison with international regulators and standard setting bodies will also be required.

<sup>30</sup> p. 35 of the NT Policy Document.

## Consumer education and awareness

As explained earlier, one of the primary reasons for introducing a TCF framework in South Africa is the asymmetry of information between retail financial services consumers and financial institutions, and the consequent vulnerability of financial services consumers to unfair treatment. Although effective regulation of TCF rules and principles is necessary to reduce the risks inherent in this asymmetry, the only way to reduce the asymmetry itself – and so place retail customers in a fairer bargaining position in relation to financial firms - is through increasing consumers' financial literacy levels. This is a long-term strategy.

The NT Policy Document proposes the development of a national financial literacy strategy, an action plan for its implementation and “a clear assignment of roles and responsibilities of key stakeholders including the market conduct regulator”<sup>31</sup>. Clearly therefore, it will be important for the TCF fairness outcomes and the key features of the TCF regulatory framework, to be appropriately incorporated into the national financial literacy strategy. The delivery of TCF will be strengthened if customers are aware of:

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

Accordingly, although “consumer financial education is not a substitute for effective consumer protection and market conduct regulation”<sup>32</sup>, it has an important role to play in supporting TCF's ultimate desired outcomes. The FSB will therefore seek to drive consumer awareness of TCF as part of its broader consumer education initiatives, which in turn will be aligned to the development of the national strategy. The national strategy will entail a co-ordinated multi-stakeholder approach, involving government, schools, financial institutions, industry associations, employers, trade unions, community organisations and non-governmental organisations. The FSB will identify appropriate opportunities to include TCF messaging in its consumer education initiatives with these stakeholders.

In addition, the FSB has and will continue to seek opportunities to drive awareness of TCF through the national consumer media and through presentations at appropriate conferences and other speaking engagements.

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<sup>31</sup> p. 48 of the NT Policy Document

<sup>32</sup> p. 48 of the NT Policy Document

## CHAPTER 8:

# Next steps

Chapter 9 sets out the various steps in the development and implementation of the TCF framework, in the form of a timeline. This Chapter 8 provides further detail of some of the key immediate next steps, to be conducted during the remainder of 2011.

### **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.<sup>33</sup> It will comprise specific questions to enable firms to evaluate their TCF readiness, both against specific expectations on a numerical scale, as well as through qualitative questions aimed at eliciting further information regarding the firm's practices and operations.

#### ***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. The FSB will invite approximately 20 to 25 firms to participate in the pilot exercise. Participants will comprise a sample of different types of regulated firms, ranging from large conglomerates to smaller "niche" firms. Types of firms will include long-term and short-term insurers, collective investment scheme management companies, pension fund administrators, and financial services providers (including discretionary and administrative FSP's). Small and medium sized "Category 1 FSP's"<sup>34</sup> will not be included in the pilot exercise, although the intention is to include a selection of larger "Category 1 FSP's" who are not also product suppliers.<sup>35</sup>

<sup>33</sup> See Chapter 2 for details of the TCF outcomes and culture framework.

<sup>34</sup> "Category 1 FSP's" refers to financial services providers licenced as such in terms of the "Determination of Fit and Proper Requirements for Financial Services Providers" (BN 106 of 15 October, 2008, as amended), published under the FAIS Act, 37 of 2002.

<sup>35</sup> Smaller Category 1 FSP's will be excluded from the self-assessment pilot for risk-based and capacity constraint reasons. This does not however imply that these FSP's will not be expected to

The basis for selecting participants in the pilot exercise will be to:

- ensure an appropriate mix of participants that can provide insight into the suitability of the tool for different industry sectors and different firm sizes; and
- identify participants who will be willing and able to provide meaningful, practical input into the effectiveness of the tool, based on TCF preparation work they may already have carried out.

The intention is to provide invited pilot participants with the draft questionnaire and allow them a reasonable amount of time to submit completed questionnaires to the FSB. The FSB will then conduct separate in-depth interviews with the pilot participants to obtain feedback on the utility of the tool, any difficulties in answering the questions and suggestions for improvement of its structure and content. The self-assessment tool will then be refined in light of the feedback received from the pilot group, and a revised tool developed and distributed for general industry use.

The target timeline is to identify pilot participants and provide them with the draft self-assessment tool by June 2011, conduct follow-up interviews in July 2011, and make the revised tool available for broader industry use in August 2011.

#### ***Limitations of the self-assessment tool***

It is important for firms to appreciate, as the FSB does, that although the self-assessment tool will hopefully serve a useful purpose in aiding TCF implementation and understanding, it cannot serve as a definitive “template” to guarantee full compliance with TCF accountabilities. More particularly:

- The TCF tool will, at least initially, be prepared on a “one size fits all” basis, for use by all regulated firms. As such, it cannot and will not take into account a firm’s specific strategies, business model, operational structure and unique conduct risks. To ensure accurate and comprehensive TCF self-assessment, firms should therefore develop their own self-assessment methods, using the FSB’s tool as guidance where appropriate.
- Firms must take care not to regard the questions asked in the self-assessment tool as an exhaustive “checklist” of the areas the FSB will focus on in monitoring and assessing TCF delivery. The revised supervisory and enforcement approaches outlined in Chapters 4, 5 and 6 will mean that the FSB will require detailed TCF reporting information from firms and focus more intensively on firm-specific conduct risks. The FSB will in no way limit its supervision of firms to items included in the self-assessment tool. Demonstrating a “good TCF score” using a generic self-assessment tool will therefore not guarantee a “clean bill of health” on TCF from the regulator, in the absence of demonstrable firm-specific evidence of achievement of the TCF outcomes.
- The self-assessment tool is precisely that – a “self” assessment. There is therefore a risk that firms will provide subjective responses to the self-assessment questions, and be lulled into a false sense of security regarding the assessment results. It is essential to bear in mind that, before a firm (or the regulator) can place any reliance

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deliver TCF outcomes. See the discussion regarding the application of TCF to FAIS regulated intermediaries in Chapter 4.

on a self-assessment every response provided must be capable of being substantiated by measurable MI or other objective supporting evidence.

- Achievement of TCF outcomes cannot be reduced to a mathematical exercise. To the extent that the self-assessment tool provides a “scoring” methodology, this is only for purposes of allowing firms (or the regulator, where applicable) to use it as a benchmark against which future TCF delivery improvement (or deterioration) can be measured and responded to. A high numeric score should not be regarded as an absolute measure of TCF success. Delivering TCF outcomes will require ongoing effort and cannot be seen as a once-off event that can be “ticked off” as completed.

## **The TCF benchmarking exercise**

Some of the feedback provided on the TCF Discussion Document was that it was unclear how the success of TCF would be measured. The following question arises: Given that TCF will not be entirely rules-based, but will include principles-based and culture change components, how will the FSB and other stakeholders know whether or not the TCF initiative has been successful in delivering its desired outcomes?

As mentioned under the discussion on the TCF self-assessment tool, achievement of TCF outcomes cannot be reduced to a mathematical exercise. Nevertheless, the FSB does believe that it would be useful to attempt to take an initial snapshot of how current customer treatment practices measure up against the six fairness outcomes. This snapshot can then be used as a benchmark – albeit approximate – against which to assess future progress in delivering TCF outcomes.

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 benchmarking exercise will entail the completion of the self-assessment tool questionnaire by a sample of identified regulated firms and submission of the results to the FSB for collation and aggregation. The size and composition of the sample is still to be decided, although it is envisaged that the sample will be substantially larger than the sample used for piloting the self-assessment tool. The aggregated results of the benchmarking exercise will be made publicly available. The target is to commence the benchmarking exercise in August and September 2011, after publication of the self-assessment tool, with a view to publishing the results in early 2012.

Insights obtained from firms in completing the self-assessment tool questionnaire, both for the pilot and benchmarking exercises, will also be useful in helping to identify current TCF weaknesses in the industry or specific sectors. These insights will in turn inform the development of the regulatory, supervisory and enforcement frameworks.

## **Stakeholder engagement strategy**

In addition to the self-assessment pilot and the TCF benchmarking strategy, a process of identifying and engaging stakeholders to participate in the further roll-out of TCF will also commence shortly after publication of this Roadmap.

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 Steering Committee's mandate will be formalised. Working groups will also be established under the oversight of the Steering Committee, to support the development of the various regulatory themes that will make up the overall regulatory framework, as discussed in Chapter 5.

The target timeline is to have the TCF Regulatory Steering Committee in place by end May, 2011. The setting up of working groups and sequencing of thematic regulatory proposals will need to be agreed by the Steering Committee once convened. As mentioned in Chapter 4, a proportionality principle will be applied in developing the regulatory framework. Proportionality will also inform the sequencing of implementation, with staggered implementation timelines and possibly tiered standards being applied to different categories of firms, depending on the conduct risks identified.

The overall target is to produce a complete TCF regulatory framework proposal for approval by the National Treasury (and the Council of Regulators, to the extent required) in the last quarter of 2012. Normal legislative consultation, deliberation and approval processes will then follow to promulgate final legislation and subordinate legislation, as the case may be.

The overall regulatory framework timeline does not, however, preclude the promulgation of interim legislative or regulatory changes relevant to TCF from time to time, where these may be necessary to respond to particular market conduct concerns, or form part of existing legislative review processes that are already in the pipeline.

As mentioned elsewhere in this Roadmap, over and above the work of the TCF Regulatory Framework Steering Committee, the FSB will initiate other stakeholder engagements necessary to develop broader elements of the TCF framework and its supporting structures.

# CHAPTER 9:

## TCF timeline

The timeline diagram on the next page sets out the sequencing of the key steps in rolling out the TCF model and some target dates. While it is possible that the sequence of the TCF outputs may be modified slightly as the process unfolds, and target dates may shift due to external dependencies, the FSB is committed to the full implementation of TCF and its vision of a future where the South African financial services industry can be noted for its commitment to treating customers fairly.

TCF Roadmap Timeline	Q2 2011			Q3 2011			Q4 2011			Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013
	A	M	J	A	S	O	N	D									
<b>PILLAR 1: The TCF framework</b>																	
<b>1.1 Regulatory Framework (1)</b>																	
Establish TCF Regulatory Framework Steering Committee (SC)																	
Agree themes and high level scope																	
Establish SC working groups																	
Regulatory alignment analysis																	
Draft & publish legislative proposal discussion documents																	
Consult stakeholders on discussion documents																	
Develop final legislative recommendations																	
Consult with NT and Council of Regulators for approval																	
Formal legislative processes																	
Legislative implementation - Jan 2014 (2)																	
<b>1.2 Supervisory framework (3)</b>																	
Develop internal FSB framework																	
FSB skills and capacity analysis																	
FSB capacity building																	
Develop and publish TCF supervisory framework																	
<b>PILLAR 2: Implementing TCF</b>																	
<b>2.1 TCF Self-assessment tool</b>																	
Identify pilot participants & distribute pilot self-assessment tool																	
Pilot participants submit completed questionnaires																	
Interview pilot participants																	
Stakeholder input																	
Publish final self-assessment tool for industry use																	
Provide feedback to pilot participants																	
<b>2.2 TCF Benchmarking exercise</b>																	
Identify benchmark participants & distribute self-assessment tool																	
Benchmark participants submit completed questionnaires																	
Collate & analyse benchmark data																	
Publish benchmark exercise findings																	
<b>2.3 Guidance</b>																	
FSB publishes guidance notes as need for them is identified																	
<b>2.4 TCF Annual report</b>																	
Include TCF in 2011 FSB Annual Report and annually thereafter																	
<b>PILLAR 3: Incentives &amp; deterrence</b>																	
<b>3.1. Reporting requirements (4)</b>																	
Develop initial non-public reporting requirements																	
Develop final non-public reporting requirements																	
Develop public reporting requirements																	
Firms begin prescribed TCF reporting (public and non-public)																	
<b>3.2. Enforcement</b>																	
FSB begins pro-active intervention for identified TCF conduct risks																	
FSB begins formal TCF enforcement - Jan 2014 (5)																	
<b>Supporting Structures (6)</b>																	

**Notes:**

1. This timeline does not preclude earlier promulgation of TCF related legislative changes where these may be necessary to respond to particular market conduct concerns or form part of legislative reviews already in the pipeline.
2. Implementation dates are dependent on the legislative process.
3. Development of the TCF supervisory framework, as part of the FSB's broader market conduct mandate, will be appropriately aligned to the development of the "twin peaks" regulatory model proposed in the NT Policy Document.
4. The final prescribed reporting requirements (public and non-public) will form part of the TCF supervisory framework. Prior to publication of the final reporting requirements, the FSB will develop initial reporting requirements which firms will be required to submit from time to time, to be used as input into the final regulatory and supervisory frameworks.
5. This is based on the January 2014 target implementation date for the regulatory framework legislative changes. Where unfair customer treatment constitutes a breach of existing regulation or legislation, formal enforcement action can take place at any time.
6. Ombud schemes and other market conduct regulators will be engaged at all relevant stages of the TCF roll-out. The FSB will on an ongoing basis use appropriate media and industry platforms to increase consumer and stakeholder awareness of TCF initiatives.

## Annexure A:

### Review & feedback on comments received on the FSB's "*Treating Customers Fairly*" Discussion Document (April 2010)

In April 2010, the Financial Services Board published a discussion document entitled *Treating customers fairly*, in which it sets out the motivation and brief history of the TCF approach and provided some practical examples of its application in South Africa. Industry stakeholders and experts were invited to comment on the document.

#### **Overview of feedback received**

A total of 25 written comments were received from individuals, firms, industry bodies and ombud schemes in the financial services industry. In general the comments were positive towards TCF and the role it could play in driving positive outcomes for retail financial services customers and the industry as a whole.

Many of the comments revolved around questions of scope, definition and classification. In particular, commentators asked for clarity on the institutions, customers and products and services that would be included in the ambit of the TCF model. Concerns were also raised regarding gaps or overlaps as far as existing legislation is concerned.

Comments were also received regarding whether it was feasible or necessary to define "fairness", and if so how this should be done.

Other matters that arose from the comments have to do with the approach of the FSB to implementation and the processes envisaged and questions related to supervision and enforcement.

#### **Main categories of comments and the FSB's responses**

The comments received were wide-ranging in nature, but shared certain elements. In the headings that follow, issues that share similar themes and the FSB's responses to these issues, will be grouped together.

A number of the issues raised have been addressed in the main body of this Roadmap, so the responses will therefore include references to applicable parts of the Roadmap.

***Who is a “retail customer” and what are “retail financial services”?***

The “C” in TCF is intended to refer to ordinary financial services customers who would typically be vulnerable to unfair treatment as a result of having unfair bargaining power and asymmetrical access to information, as compared to financial firms. As such, it is not limited only to protection of natural persons and should also ensure fair treatment of juristic entities that have these vulnerabilities. Chapter 4 discusses the pro’s and con’s of explicitly defining “retail” for TCF purposes and suggests that this be the subject of further discussion.

***Which regulated firms and activities will be required to deliver TCF outcomes?***

Related to the question of who is a retail customer, is the question whether TCF is only intended to apply to firms who engage directly with “end user” retail customers, and what role other firms in the value chain – e.g. “wholesalers” – should be expected to play in delivering TCF outcomes. This question is discussed in Chapter 4. While TCF relates specifically to retail or end-user customers, this does not obviate all those who sell products or services wholesale from the TCF regime. This is a good example of the fact that the TCF approach affects the entire product life cycle. Chapter 4 explains that a sensible approach will be required in drawing lines of responsibility between different firms in the value chain of an end retail product and that guidance will be provided in due course.

Comments and questions were also received regarding the application of TCF to specific categories of firms, namely: FAIS regulated intermediaries, retirement funds and the retail banking industry. The FSB’s response to these comments is as follows:

- **FAIS regulated intermediaries:** Although clearly the FAIS Act already imposes a number of obligations on authorised financial services providers and their representatives that are relevant to TCF, this does not mean that TCF will have no additional impact on them. Intermediaries, like other regulated financial firms, will need to demonstrate the adoption of a TCF culture and the delivery of TCF outcomes for their customers. Chapter 4 discussed this in more detail, and explains some of the ways in which the responsibility for fair treatment of their mutual customers will need to be shared by intermediaries and product suppliers.
- **Retirement funds:** The scope of TCF for the retirement fund industry is a good example of the debates that can arise regarding “wholesale” and “retail” activities. It seems clear that individual retirement offerings such as retirement annuity and retirement preservation funds must be regarded as “retail” business for TCF purposes. However, a complex set of legal relationships exists between the participants in the retirement product value chain and further work is needed to test the application of TCF to both these and other retirement product structures. Chapter 4 deals with this issue in more detail and confirms that engagement with stakeholders will take place.
- **Retail banking industry:** Feedback on the TCF Discussion Document included opposing views on whether or not TCF should apply to the banking sector. Views ranged from recommendations that the banking regulator be engaged to ensure

that a similar model would be applied for the benefit of retail banking customers, to recommendations that banks be explicitly exempted from the TCF programme. These recommendations were however based on the premise of the current financial services regulatory model, where the FSB does not have regulatory jurisdiction over the banking sector – other than to the extent that banks render services subject to the FAIS Act or have entities within their groups that offer FSB regulated non-banking products. Since then, the National Treasury has published the NT Policy Document discussed elsewhere in this Roadmap. It has been confirmed that, under a “twin peaks” regulatory model, the FSB’s market conduct mandate will be expanded to include the retail banking sector. Therefore, although in the initial phases of implementation, the TCF framework will not yet cover the retail banking sector, it is expected that banks will in time fall under the broader TCF umbrella as the details of the “twin peaks” model are settled.

In summary, *all* financial firms regulated by the FSB- including, in time, the retail banking sector - will be under TCF scrutiny. Currently this includes long-term and short-term insurers, collective investment schemes, pension funds, friendly societies, financial services providers (including discretionary and administrative FSP’s), and entities falling within the jurisdiction of the JSE and STRATE<sup>36</sup>. The actual TCF deliverables expected of these firms – particularly where they do not interact directly with retail consumers - will however be the subject of further engagement, informed by a risk-based and proportional regulatory approach.

#### ***How will gaps and overlaps with other legislation be addressed?***

Understandably, many commentators highlighted the need for the TCF framework to take account of existing legislation and regulation to avoid overlaps, gaps and inconsistencies. A number of specific items of existing legislation were flagged – particularly the FAIS Act. As explained in Chapter 4, the FSB recognises that the TCF regulatory framework must aim for consistency, completeness and co-ordination. The chapter also sets out details of the process that will be followed in developing the regulatory framework, including the establishment of a TCF Regulatory Steering Committee comprising key stakeholders, a comprehensive regulatory alignment analysis, and co-ordination with other regulators. A non-exhaustive list of current legislation that will be assessed – both FSB regulated and non-FSB regulated – is provided. The gap-overlap analysis will not only relate to how the existing regulations address fairness, but also the extent to which they allow for monitoring and enforcement by the FSB. Some commentators also pointed out that there are existing industry standards and codes that incorporate fairness in one way or another. Chapter 4 mentions that consideration will be given to the role industry association standards can play in reinforcing the delivery of TCF outcomes by their member firms, with reference to their likely effectiveness and competition law considerations.

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<sup>36</sup> See further discussion on these entities in Chapter 4.

***What is “fairness” and can – or should – it be regulated?***

Some commentators pointed out the challenges in seeking to define, and regulate, the concept of “fairness”. The FSB’s view is that the focus on clearly articulated, measurable and demonstrable fairness **outcomes** obviates the need to separately define “fairness” itself. While firms may have different definitions of fairness - in the same way that they have different cultures - the FSB is concerned with the outcomes that those definitions deliver and whether the firm can demonstrate that it has a framework for assessing and maintaining the desired outcomes. Put simply – the FSB’s “definition” of fairness for purposes of the TCF framework is demonstrable delivery of the six fairness outcomes.

However, to consider the broader conceptual question of whether fairness can be regulated, it may be useful to compare a TCF approach with the issue of road deaths and the existence of speed regulations. In making such a comparison one sooner or later has to consider the efficacy of the legal system, matters of deterrence and the mindset of participants. If, for example, motorists feel it is socially acceptable to exceed the speed limit, how can such attitudes be changed?

It has been argued that any attempt to force firms (via legislation) to treat customers fairly runs into the problem that one cannot legislate ethics. Consider the following two statements: (1) You must treat your customer fairly; (2) You must not treat your customer unfairly. Arguably, even if legislation to promote fair behaviour (the first statement) is unlikely to have any effect, legislation can effectively be introduced to deter unfair behaviour (see the second statement).

***How will the FSB implement TCF?***

This question is addressed in Chapters 4 and 5 of the Roadmap, which provide details of the TCF regulatory and supervisory frameworks to be developed, and the new structures both firms and the FSB will need to put in place to ensure successful implementation of TCF.

***How will the FSB supervise and enforce TCF?***

This question is addressed in Chapter 6. It discusses the reporting obligations – both public and non-public – that firms will need to meet to demonstrate TCF delivery and enable the FSB to monitor such delivery, as well as the range of enforcement mechanisms available to the regulator.

***Will TCF apply “retrospectively”?***

A particular question that arose in regard to TCF enforcement was whether the TCF approach would be “retrospectively” applied to historic (“legacy”) products and practices. Concerns were expressed regarding the consequences of applying current norms to past practices, which may have been developed in very different environments and contexts.

TCF is a new, forward looking regulatory approach and is not intended to focus on redress for historic practices. However, this does not mean that firms may with impunity continue to

market products and services that have negative customer outcomes, on the basis that these products and services were designed prior to the introduction of the TCF regulatory model. Firms will be expected to review their current product and service offerings against TCF standards, and take appropriate action if they find that TCF outcomes are not being delivered.

It also does not mean that, in evaluating whether customers are today being treated fairly, those customers who happen to hold products that were developed and purchased yesterday, are not entitled to fair treatment. In this regard, fairness outcome 5 (*Customers are provided with products that perform as firms have led them to expect*) must be emphasised. Firms will be expected to deliver TCF outcomes to all their customers – including holders of legacy products. Where it becomes apparent that products sold in the past are not meeting – or are no longer meeting – the expectations initially created, firms will be expected to identify reasonable ways to improve outcomes for their customers.

The FSB will also, as part of the proactive supervision approach outlined in Chapter 5, engage with firms to find appropriate solutions to any identified unfair outcomes arising from legacy products and practices.