Conduct Standards for Banks 2020

Thought Leadership

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What is this Standard?

> The objective of the Conduct Standard is to introduce requirements that promote the fair treatment of financial retail customers.

The standard was promulgated by the Financial Sector Conduct Authority (FSCA) under the Financial Sector Regulation Act 2017 (FSRA) in respect of banks, mutual banks and co-operative banks. Banks will be required to demonstrate to the FSCA that fair outcomes for customers are being consistently delivered in the provision of financial products and services. There will be an emphasis on pre-empting and remediating negative customer feedback, hence the FSCA will be using proactive supervisory approaches to address any risks associated with misconduct.

The Conduct Standards

The standards were designed to follow the sequencing of the six (6) Treating Customers Fairly (TCF) Outcomes and the requirements set out in the standards were directly informed by the TCF Outcomes, with the following additional expectations from each:

TCF OUTCOME 1

Banks are expected to demonstrate that fair customer treatment is central to their company culture and this would include embedding governance and oversight frameworks. The bank's governance arrangements must provide for regular risk-based monitoring and evaluation of the adequacy of the banks systems and processes.

TCF OUTCOME 2

Banks are required to regulate the design, suitability and performance requirements for financial products and financial services keeping in mind the interests of its customers. This must include the oversight arrangements that a bank must have in place in order to meet these objectives.

TCF OUTCOME 3

Certain disclosures must be made to a customer of the bank so as to ensure that the customer is aware of and understands all the relevant facts related to the product/service. These are facts that could reasonably be expected to influence the financial customer's decisions relating to the financial product or financial service.

TCF OUTCOME 4

Banks need to take into account certain factors when making disclosures to customers, such as the nature and complexity of the financial product. This is to ensure that a customer is given appropriate information about a financial product/service at the point which the information will be most useful to the customer's decision-making in relation to entering into, using, or maintaining the product or service. Product advertisements need to be clear, fair and not misleading. Banks are responsible for the oversight and compliance thereof of 3rd party advertising service providers.

TCF OUTCOME 5

Banks must be aware of and apply the standards for the prohibition of unfair product terms and conditions, including additional product design standards applicable to this market segment. This part of the Conduct Standards is only applicable to retail customers

TCF OUTCOME 6

A bank is required to establish a complaints management framework, and establish appropriate training of responsible staff, the categorisation of complaints and other procedures relating to complaints. This part of the conduct standard also deals with account closures and account switching, whether initiated by the financial customer or the bank themselves.

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Why are these standards important?

Since the 2007/2008 financial crisis, a global reform shifting focus to the importance of market conduct has taken place. In South Africa, the past decade various enquiries and reports have highlighted a number of mis-conduct events within the banking sector

Notably the Banking Enquiry (part of the Jali Commission) made a number of findings and recommendations with regards to poor customer outcomes being experienced by the customers of retail banks. This emphasised the gap in the regulation of market conduct of retail banks. In more recent times 2016/2017, the National Treasury commissioned the World Bank to undertake a "Retail Banking Diagnostic".

The aim was to identify potential deficiencies from a fair-treatment perspective in banks' provision of transactional and fixed deposit accounts to customers. The diagnostic report also included recommendations on how any identified fair-treatment deficiencies could appropriately be addressed through market conduct regulation, considering international good practices and the South African market context. The Retail Banking Diagnostic report was finally issued in 2018 with various recommendations to be considered and implemented.

South Africa has followed in the footsteps of other countries where their market conduct regulation is more mature and certain lessons can be learnt.

An example is the Australian "Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry" where key focus areas in assessing misconduct were identified:

- **Culture practices:** Organisations must invest heavily in developing a strong and ethical culture that is aligned to the purpose of the organisation, with boards and senior management setting the tone from the top. Directors are expected to develop tools and systems to monitor and assess organisational culture, in place of waiting for the regulators to make impactful changes.
- **Governance practices:** as a priority, boards need to:
  - **Review organisational, management and governance structures -** to clarify role definition, management breadth and accountability to ensure these are not causing poor customer outcomes.
  - **Take ownership for non-financial risks -** boards must look at a broader range of non-financial risks, including reputation, brand, sustainable performance and innovation, to assure good customer outcomes are being delivered.
  - **Measure and monitor culture and customer outcomes -** boards must measure and monitor culture (through lead and lag indicators) and the value delivered to customers.
  - **Use consequence management to enforce accountability -** boards must hold senior management to account for delivering on strategy in a way that is ethical, sustainable and aligned to principles.
  - **Empower employees to focus on good customer outcomes -** organisations need to use their governance framework to encourage principle-based decision making, asking "Should we?" in moments that matter.
- **Remuneration and recruitment practices:** Remuneration is a key lever to enforcing business behaviours. To prevent remuneration from encouraging misconduct, it was suggested that enhancements to existing regulatory bodies or frameworks, including proposing remuneration framework design changes to be integrated in revised Prudential Standards.

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Challenge: Principle vs Rule based

The Banking Conduct Standard effectively balances principles-based requirements (where Banks are guided by their own principles, policies and procedures); and rules-based requirements (what Banks promise is what customers get), to ensure that they deliver fair customer outcomes in a disciplined, transparent and consistent manner.

Banks will be expected to design and implement appropriate governance policies and other control mechanisms that will ensure that fair treatment of customers is central to their organisation.

Banks will also be required to demonstrate to the FSCA that fair outcomes for customers are consistently delivered when providing financial services and financial products to customers.

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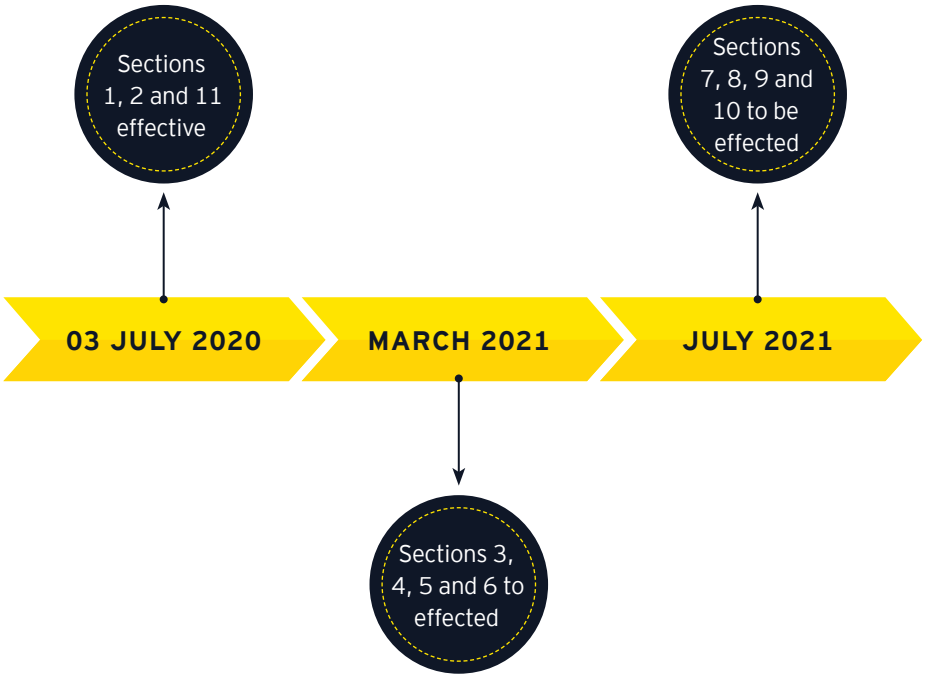
Compliance timeline



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How can EY help you?

The Conduct Standards although considers a phased in implementation, South Africa's financial institutions will be required to implement these standards in all aspects of their business.

"We found an issue with a financial product or service and may need to make a change that could affect customers"

"We aren't sure if we are compliant with regulatory requirements and need to provide assurance"

Various EY client queries

"We need to work out what new regulation means for our business and how we get compliant"

"We are working on our conduct framework and doing work on culture but are finding it difficult to align the two"

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How can EY Help

EY has a dedicated Financial Services Consulting practice, which includes Risk Management, Technology, Process and People. This gives us deep industry knowledge in all aspects of the financial services industry, allowing us to tailor integrated solutions to our clients' specific needs.

Our Financial Services Risk Management (FSRM) practice, which forms part of the Financial Services Risk domain in Business Consulting, is experienced within financial services firms and regulators in various jurisdictions and composes of a variety of skills across the insurance and banking sectors. We combine local regulatory and legislative knowledge with best practices in global prudential regulation as well as governance,risk and compliance (GRC).

Through our fully integrated global Prudential, GRC and Actuarial networks, we ensure that we are at the forefront of global regulatory developments. We leverage this to approach compliance and risk management not only from a regulatory perspective, but also from a strategic perspective.

Market Conduct:

The FSRM team can assist in helping financial services organisations design their interactions with customers and counterparties, to deliver fair outcomes and market integrity, and effectively manage associated regulatory, reputational and strategic risks. We can do this by:

- Assisting our clients with the design and development of market conduct frameworks, organisational culture frameworks and assist in implementation thereof, and
- Performing gap analyses against the regulatory requirements and benchmarking compared to local and global practice of existing market conduct frameworks.

Governance, Enterprise Risk and Compliance:

Within the GRC space, our FSRM team can assist in:

- Reviewing Governance Policy and Control Adequacy,
- Assessing the maturity of Risk / ERM and Compliance
- Functions (including benchmarking to best practice),
- Developing or assessing 3rd Party Risk and Binder Risk Management Frameworks,
- Designing, implementing or enhancing Credit Risk Frameworks,
- Establishing ESG governance frameworks and design disclosure,
- Developing, implementing or enhancing Model Risk Management,
- Setting up or reviewing Recovery and ResolutionPlanning,
- Assisting in preparing for the requirements under the Financial Conglomerate Supervision/Regulation,
- Assisting in selecting GRC solutions and implementingthese, and
- Establishing and management of Regulatory Inventories and risk controls.

Prudential Risk:
The services offered to banks and insurers include:

- Reviewing Regulatory Capital Requirements (BA Returns and Quantitative Returns),
- Reviewing or performing ICAAP/ORSA,
- Assisting in Capital and Balance Sheet Optimisation/Management,
  - Developing Economic Capital models,
  - Performing reviews of Pillar 3 Requirements for Banks,
  - Supporting in IBOR/JIBAR transition implications and preparation,
  - Optimisation of overall financial resources

- EY can assist with defining the prudential regulatory framework and the pro-active strategic response to mitigate the implications of these regulations on key financial indicators.
- EY's global regulatory network leverages regulatory knowledge on an international scale. We can support our clients in understanding and addressing the most critical financial and compliance impacts for their business as a result of regulatory change and help them to implement solutions on a cross-border basis to support compliance wherever they operate.
- In today's environment of heightened and evolving regulation and structural changes, our professionals can work side by side with our clients to interpret new rules as they are issued. Through this collaboration, any compliance and operational changes that are required can be identified quickly and processes can be established to implement them efficiently.

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Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

Creative Services ref. 6742. Artwork by J Aricksamy.

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