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Market conduct regulation of complaints management in the insurance industry

by

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Abstract

Since 2012, the financial sector regulators have been engaging with the industry on the regulatory framework, specifically the policyholder protection rules (PPR) and Treating Customers Fairly (TCF) approach. The purpose of the adoption of these principles is to ensure the fair treatment of customers. The approach seeks to ensure fair outcomes to customers within the financial services sector and to ensure that the sector is adequately regulated at all stages in the relationship between the institution and its customers.

During these engagements, it became clear that the current financial services regulatory framework in relation to complaints management was deficient. The purpose of the proposed changes to the complaints management framework was to effect a more consistent and comprehensive regulatory framework to support the delivery of the specific outcomes envisaged for complaints management across different types of financial institutions.

In order to develop proposals, the Financial Services Board carried out a thematic review of complaints handling practices from April to June 2014. The findings arising out of the thematic review were aimed at encouraging insurers to assess the effectiveness of their complaints management processes and, where necessary, effect improvements to, or enhance, their complaints handling methodologies.

There is a need to unpack complaints management in the insurance industry and to research possible improvements on deliverables relating to market conduct. Complaints management is a core component of market conduct-related behaviour and regulation. The dissertation evaluates the South African system against foreign jurisdictions' frameworks for complaints management and international best practices in order to show the need for improvement and make suitable recommendations. Against this background, the dissertation considers the following research questions:

1. What is the current regulatory framework in South Africa that governs complaints management?
2. How does the South African insurance industry deal with the recent regulatory changes, specific to complaints management?
3. What are the challenges that exist within the current complaints management framework in its state of implementation, and will future law change these practices?

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4. What are the practices endorsed by the regulators in respect of complaints management in South Africa and other countries, specifically the UK and are there international best practices that exist in this regard?
5. How can the South African insurance industry align with national and international best practices relating to complaints management and in terms of regulatory changes within the complaints management framework?

The research finds that there are still many questions and concerns relating to complaints management. Amongst other findings, there is a need for greater engagement between the industry and the Regulator, an exercise of education for not just the financial services customer, but for the financial services institution, as well. The need for standardization and consistency was a requirement which was much needed. Whilst it is noted that there is a separate market conduct regulator, it is clear that there should be effective coordination to ensure a sustainable model in future.

The research seems to have raised a number of unanswered questions – not all of which fall within the ambit of legal scholarship (such as the cost-impact of the regulatory changes to complaints managements). A number of areas were identified as key areas of concern within complaints management which will require constant monitoring, review and research in order to ensure that complaints management complement market conduct outcomes as envisaged.

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Table of Acronyms and abbreviations

Acronym/Abbreviation	Meaning
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
CBRs	Conduct of Business Returns
COFI	Conduct of Financial Institutions
FAIS	Financial Advisory and Intermediary Services Act (SA)
FCA	Financial Conduct Authority
FSB	Financial Services Board
FPC	The Financial Policy Committee
FSCA	Financial Services Conduct Authority
FSMA	Financial Services and Markets Act (UK)
FSRA	Financial Services Regulation Act (SA)
PA	Prudential Authority
PRA	Prudential Regulation Authority
OLTI	Ombudsman for Long Term Insurance
OSTI	Ombudsman for Short Term Insurance
PPRs	Policyholder Protection Rules
TCF	Treating Customers Fairly

Selected core definitions

A complainant is

> "a person who has submitted a specific complaint to a financial institution or, to the knowledge of the financial institution, to the financial institution's service provider and who –
>
> (a) is a customer or prospective customer of the financial institution concerned and has a direct interest in the agreement, product or service to which the complaint relates; or

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(b) has submitted the complaint on behalf of a person mentioned in (a), provided that a prospective customer will only be regarded as a complainant to the extent that the complaint relates to the prospective customer's dissatisfaction in relation to the application, approach, solicitation or advertising or marketing material contemplated in the definition of 'prospective customer'."[1]

A complaint is defined as

"an expression of dissatisfaction by a complainant, relating to a product or service provided or offered by a financial institution, or to an agreement with the financial institution in respect of its products or services and indicating that –

(a) the financial institution or its service provider has contravened or failed to comply with an agreement, a law, a rule, or a code of conduct which is binding on the financial institution or to which it subscribes;

(b) the financial institution or its service provider's maladministration or wilful or negligent action or failure to act, has caused the complainant harm, prejudice, distress or substantial inconvenience; or

(c) the financial institution or its service provider has treated the complainant unfairly and regardless of whether such an expression of dissatisfaction is submitted together with or in relation to a customer query."[2]

"Customer" means a customer of a financial institution and "financial institution" means a licensed life or non-life insurer.

"Regulator" means the Financial Services Conduct Authority or the historic Financial Services Board.

"Ombudsman" has the meaning assigned to it in the –

(a) Financial Services Ombud Schemes Act, 2004 (Act No. 37 of 2004) up until such time as such Act is repealed through Schedule 4 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017); and

(b) Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) from the date on which such Act repeals the Financial Services Ombud Schemes Act, 2004 (Act No. 37 of 2004) through Schedule 4 of such Act.

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[1] *Ibid.*
[2] FSB *TCF complaints management* 3.

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Chapter 1: Introduction

1.1. Background to the study

There are several factors which impact the fair treatment of customers within the financial services industry, specific to insurance.[3] Included in these are market failures, a financial institution's incentives, and general customer behaviour.[4] The general issue is that financial institutions are in possession of information, whilst the customers are not.[5] This places a financial institution at an advantage which could potentially result in unfair customer outcomes.[6]

One of the greatest concerns within the financial services industry was the fact that low end customers in terms of income were purchasing sophisticated financial services products.[7] Upon these customers laying claim against a benefit, there was a repudiation of the claim.[8] This posed several concerns from a regulatory perspective.[9] The concerns were in relation to whether customers understood what they had purchased and could gauge whether financial institutions had taken advantage of the lack of sophistication within this market segment and sold financial services products or services which did not meet the customers' needs.[10] A further area which required attention was customer education.[11] If customers had adequate knowledge and understanding, they would be in a position to better understand whether a financial services product or service would be suitable to their needs.[12]

Insofar as the insurance industry was concerned, the regulatory framework came under review following the financial crisis.[13] The purpose of the review and reform was to strengthen the financial system, support economic growth and ensure fair outcomes to customers.[14] Several

[3] Feasibility *A report prepared for the FSB, TCF complaints management* 1.
[4] *Ibid.*
[5] *Ibid.*
[6] *Ibid.*
[7] *Idem* at 3.
[8] *Ibid.*
[9] *Ibid.*
[10] *Ibid.*
[11] *Ibid.*
[12] *Ibid.*
[13] Treasury *A safer financial sector to serve South Africa better* 23.
[14] *Ibid.*

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considerations were borne in mind when considering the revised regulatory regime – specifically that market conduct oversight had to be strengthened.[15]

Its purpose was to support and strengthen complaints management frameworks and the ombudsman systems to ensure that they are in a position to adequately support market conduct outcomes.[16] As such, these frameworks were reviewed in order to adequately understand the successes and challenges within the existing complaints landscape.

The Financial Services Regulator (in the style of the Financial Services Board) embarked on a thematic review from April to June 2014 in order to establish how the industry handled complaints and to understand how customers were treated in this regard.[17] The findings arising out of the thematic review were aimed at encouraging insurers to assess the effectiveness of their complaints management processes and, where necessary, effect improvements to, or enhance, their complaints handling methodologies.[18] The initial focus was the personal lines business, in effect individual customers and small and medium-sized enterprises. The Regulator, through its review and engagements, adopted the Treating Customers Fairly (TCF) framework to ensure fair outcomes to customers within the financial services sector.[19] The intention was to ensure that the industry was adequately regulated at all stages of the relationship between the customer and the financial services institution.[20] As issues manifest prominently during the complaints process, the complaints framework came under review.

The Regulator sought to standardize all complaints management practices to ensure consistency in the application of the principles that it valued.[21] The purpose of the new regulatory approach was specifically to improve market conduct within the financial services industry and ensure the fair treatment of its customers.[22] One of these changes was the new Policy Protection Rules (PPRs) which were signed into law on 15 December 2017. This was in respect of both the short-term and long-term PPRs. The rules were intended to have a phased implementation process. The new PPRs brought about sweeping changes and affected personal lines policies as well as small commercial policies.[23] The definition of a policyholder was also

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[15] *Idem* at 24.
[16] *Ibid.*
[17] FSB *TCF complaints management* 2.
[18] *Ibid.*
[19] *Ibid.*
[20] *Ibid.*
[21] *Idem* at 1.
[22] *Ibid.*
[23] FSCA *Proposed Amendments to PPR Consultation Report 2.*

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amended to include a potential policyholder.[24] These regulations formally incorporated the six TCF outcomes into law. Of importance and relevance to complaints management is that complaint escalation processes needed to be documented and complaints procedures communicated to clients at the time of the sale of the policy, as well as at the time of the claim being handled.[25]

On 1 April 2018, South Africa began to implement its regulatory system change wherein two regulators were confirmed to be in operation: the Prudential Authority (PA) and the Financial Sector Conduct Authority (FSCA).[26] The legislation removed the Financial Services Board.[27] With this announcement, the real regulatory changes of the market conduct aspects began to unfold as the FSCA initiated its own strategy.[28] A new market conduct regulator was born with its strategy being accessible on its new website.[29] The market conduct concerns identified in the review of the complaints management practices of financial institutions illustrated that there ought to be consistency in how complaints are dealt with.[30] It was therefore a requirement to review the bodies that governed complaints management and understand their respective roles and contributions to the effective handling of complaints within the industry.[31]

1.2. Research problem and questions

Since 2012, the various financial sector regulators responsible for market conduct have been engaging with the industry on the regulatory framework, specifically the PPRs and the TCF approach. The purpose of the adoption of these principles is to ensure the fair treatment of customers. The approach seeks to ensure fair outcomes to customers within the financial services sector and to ensure that the sector is adequately regulated at all stages in the relationship between the institution and its customers.[32]

During these engagements, it became clear that the current financial services regulatory framework in relation to complaints management was deficient.[33] The purpose of the proposed changes to the complaints management framework was to effect a more consistent and

[24] *Ibid.*
[25] *Ibid.*
[26] Treasury *New Twin Peaks regulators established* 1.
[27] *Ibid.*
[28] FSCA *Regulatory Strategy* 11.
[29] Available at www.fsca.co.za.
[30] FSB *TCF complaints management* 6.
[31] FSCA *Regulatory Strategy* 11.
[32] *Ibid.*
[33] *Ibid.*

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comprehensive regulatory framework to support the delivery of the specific outcomes envisaged for complaints management across different types of financial institutions.

Notwithstanding the above, limited non-regulatory research has been conducted in the area of complaints management in South Africa. There is a need to unpack complaints management in the insurance industry and to research possible improvements on deliverables relating to market conduct. Complaints management is a core component of market conduct-related behaviour and regulation.

Against this background, the dissertation evaluates the South African system against foreign jurisdictions' frameworks for complaints management and international best practices in order to show the need for improvement and make suitable recommendations. In light of the limited academic debate on the topic, this necessitates the extrapolation of factors discussed in other phases of insurance products to complaints management.

The following research questions are considered:

1. What is the current regulatory framework in South Africa that governs complaints management?
2. What are the challenges that exist within the current complaints management framework?
3. What are the practices endorsed by the regulators in respect of complaints management in South Africa and other countries, specifically the UK, and are there international best practices that exist in this regard?
4. How can the South African insurance industry align with national and international best practices relating to complaints management and in terms of regulatory changes within the complaints management framework?

1.3. Significance of the study, delineation and limitations

As indicated above, and against the realization that complaints management support market conduct outcomes and highlight challenges in the sector, the main issues relating to complaints management were the following:

- The manner in which financial institutions handle complaints and treat their customers during the complaints management framework;

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- The level of disclosure to customers regarding complaints management processes; and
- The standardization of practices, and the consistent application of principles.

The dissertation investigates the above issues in line with the research questions. Although prudential regulation and market conduct regulation are intricately linked, the main focus is on market conduct regulation and the FSCA, as opposed to prudential regulation and the PA. In addition, data regulation will not be addressed as any analysis of information regulation should, in my opinion, form part of a separate study. The field of information regulation is complex enough on its own.

1.4. Breakdown of chapters

Chapter one sets the background for the study and orientates the reader in respect of the research problem and questions. It briefly describes the significance of the study, although this becomes clearer as the study progresses: well-designed and functioning complaints management frameworks are crucial to support positive market conduct outcomes as issues previously overlooked manifest during the complaints management process. The chapter sets the scene for the high-level evaluation of the regulatory framework for complaints management to determine whether the framework supports the intended outcomes.

Chapter two provides a high-level overview of the regulatory and legislative structure relevant to complaints management. The chapter discusses the historical development of the regulatory structure and explores why the historic structure did not meet the requirements of the foreseeable change. I then turn to deal with the regulatory reforms under the Twin-Peaks model of financial sector regulation. Chapter three builds on the structural framework depicted in chapter 2 and deals with the substance of the dissertation – complaints management in the insurance industry. I consider the challenges that relate to complaints management and discuss specific changes that the framework set out in chapter two effected to complaints management as discussed in chapter three. The chapter further provides an evaluation of the specific aspect of the policyholder protection rules as well as the guidance provided by regulators relating to expected outcomes on the complaints management framework. It provides insight into the Conduct of Financial Institutions (COFI) Bill and whether a substantial change is expected. As any discussion of complaints management would be incomplete without some reference to issues that often form the basis of disputes between insurers and customers – as non-disclosure

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and misrepresentation – I briefly refer to these against the background of chapters 2 and 3. This discussion links with the equity considerations that form part of the discussion in chapter 4.

Chapter four deals with complaints handling within the insurance industry specific to the various ombudsman schemes. It sets out the principles by which the financial services industry abides by in relation to equity and materiality to ensure fair customer outcomes. It considers the existing structure and highlights the need for a change to ensure standardized and consistent processes. Against the background of the discussion on the ombudsman scheme, chapter five evaluates the reports generated by the ombuds when discussing reporting and its relevance to complaints management. This chapter confirms that importance of data pertaining to reporting, as it enables regulators and insurers to undertake root cause analyses on trends identified, and the outcomes of decisions.

Chapter six evaluates selected aspects of the South African framework against foreign jurisdictions and international best practices and recommendations for reform. This allows for some benchmarking to determine whether there has been alignment with international trends since the new regulatory framework became operational.

Chapter seven concludes the dissertation with an overview of the salient points discussed and the provision of recommendations for reform.

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Chapter 2: A high-level overview of the regulatory and legislative structure relevant to complaints management in the insurance industry

2.1. Introduction

This chapter deals with the historic structure of the regulator, the FSB, as well as the new structure, i.e. the FSCA and PA. I will not delve into the detail of the PA, but merely confirm what its existing role is within the new structure.

2.2. Background

The greatest challenge that most countries face is that the financial sector is globally integrated yet nationally regulated.[1] It is on this basis that there was a recognition by the South African market conduct regulator of the need for minimum international standards in respect of the regulation of the financial services sector.[2]

What would this mean within the South African context and in relation to complaints management within the insurance industry? South Africa withstood the financial crisis fairly well, however, the outcomes for the customer could have been better.[3] Financial services are an integral part of the life of every South African.[4] It allows for growth, job creation, infrastructure and the development of the country and its people.[5] It is therefore important that the financial services sector is adequately regulated. Many customers within the financial services industry are not treated fairly when they are led to believe that the products or services which they purchase are of value.[6] However, the product or service that does not return the value when a claim is submitted, results in a product or service that does not meet expectations.[7] From this perspective, the market conduct concept was borne to the South African insurance industry.[8]

Market conduct regulation considers how firms within the financial sector conduct themselves, taking into consideration their clients' needs, and focuses specifically on fairness, honesty and

[1] Treasury *A safer financial sector to serve South Africa better* 9.
[2] *Idem* at 8.
[3] *Idem* at 11.
[4] *Idem* at 1.
[5] *Ibid*.
[6] Treasury *Explanatory policy paper accompanying COFI* 5.
[7] *Ibid*.
[8] Treasury *A safer financial sector to serve South Africa better* 11.

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integrity.[9] The aim is to improve outcomes for customers wherein they receive value for money on their investments.[10]

In light of the above, the following question arises: Did (and do) poor conduct practices and the poor treatment of customers within the financial sector exist?[11] Overall, the regular complaints to the various ombudsman schemes and independent studies illustrated that there was a need to review the practices of the financial services industry specific to the treatment of its customers.[12] The global financial crisis of 2008 further highlighted that there was a need for South Africa's regulatory system to be aligned with the global economy.[13] South Africa was on par with international markets from the perspective of its management of prudential risk, however, fell short when it came to market conduct risk.[14] South Africa's financial institutions were in a position to withstand the crisis, however, individual customers were not.[15] There were resultant job losses and an inability to rely on protection afforded by way of financial products.[16]

Against this background, South Africa committed to a financial regulatory reform aligned with global standards.[17] The commitment required a focused approach, which would align with four standards:

1. A stronger regulatory framework which would entail the review of existing legislation;
2. Effective supervision, which would allow strengthened Regulators to support national needs and align with international standards;
3. Ensuring that any future financial crises had minimal impacts;
4. International review, which would benchmark South Africa in order to integrate best practice standards into the national framework.[18] The increased connectivity with global markets required increased supervision to protect the South African economy as well as the South African financial services customer.[19]

[9] *Idem* at 6.
[10] Treasury *Explanatory policy paper accompanying COFI* 5.
[11] Treasury *A safer financial sector to serve South Africa better* 6.
[12] *Ibid*.
[13] *Idem* at 5.
[14] Moodley *The twin peaks model: a critical analysis of its effectiveness in SA* 48.
[15] Treasury *A safer financial sector to serve South Africa better* 5.
[16] *Ibid*.
[17] *Idem* at 4.
[18] *Ibid*.
[19] *Idem* at 5.

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What was the need for a stronger and more focused approach to financial services regulation? In general, the objectives of the reform contributed to the maintenance of financial stability, with broadened market conduct objectives of protecting financial services customers by ensuring that they have access to efficient, effective, and inexpensive financial services.[20] However, with this approach there would be exposure from a risk perspective which would require further monitoring of the financial services industry.[21]

Three examples serve to illustrate this point. First, the risk which existed, and which was of particular concern, was the high and sometimes unnecessary fees which impacted the customer.[22] This was a conduct risk in that the customer had to bear the excessive cost, resulting in lower or minimal savings to a vulnerable customer market.[23] Inevitably, the result was that the products were inaccessible to customers due to the high-cost factor associated with same.[24] The second example was alluded to earlier.[25] Unsophisticated, low income customers were purchasing sophisticated financial services products.[26] Upon these customers laying claim against a benefit – at the crucial point in time when they needed the assistance – there was a repudiation of the claim.[27] This posed several concerns from a regulatory perspective.[28] The concerns were in relation to whether customers understood what they had purchased or realized that financial institutions had taken advantage of the lack of sophistication within this market segment to sell financial services products or services which did not meet the customers' needs.[29] The third example that supports a strengthened financial services sector is the need to protect historically disadvantaged and vulnerable customers from being exploited and to ensure that they are included in the financial sector, where it is appropriate for them. It has been noted from historic data that social grant recipients for example were sold unnecessary credit and insurance contracts which they would have no use of and from which they were not able to easily exit.[30]

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[20] *Ibid*.
[21] *Ibid*.
[22] *Idem* at 6.
[23] *Ibid*.
[24] *Ibid*.
[25] See par 1.1 above.
[26] Feasibility *A report prepared for the FSB, TCF complaints management* 3.
[27] *Ibid*.
[28] *Ibid*.
[29] *Ibid*.
[30] Treasury *Explanatory policy paper accompanying COFI* 30.

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Could the practices being adopted by financial institutions be considered to be abusive? Could South Africa be exposed to increased risk due to not aligning its regulatory practices with international standards? Why fix a model which had worked effectively, and which survived the financial crisis of 2008? These were the questions being posed by the financial services industry in order to understand the need for change. The financial crisis revealed that South Africa had good prudential principles to support its survival through the crisis. The financial institutions were in a position to withstand the crisis, however as mentioned above, the aftermath from a secondary loss perspective for customers was severe.

In 2011/2012, the Regulator – known then as the Financial Services Board (FSB) – began market research on complaints management in the insurance industry.[31] The purpose of this review was to answer the very question on poor conduct practices and the poor treatment of insurance customers.[32] The market research was referred to as a thematic review, which is described as follows:

> "**Thematic reviews** are used by the regulator to 'assess a current or emerging risk relating to an issue or product across a number of firms within a sector or market' ... If specific risks are identified, further detailed work is carried out into the particular area of concern."[33]

The Regulator had been engaging with the financial services industry, including the insurance sector, since 2012.[34] The Regulator embarked on a detailed review from April to June 2014, to establish how the industry handled complaints and to understand how customers were treated.[35] The initial focus was the personal lines-business, in effect individual customers and small and medium-sized enterprises.[36] The Regulator, through its review and engagements, adopted the Treating Customers Fairly (TCF) framework to ensure fair outcomes to customers within the financial services sector.[37] The intention was to ensure that the industry was adequately regulated at all stages of the insurance relationship between the customer and the financial services institution – including at the complaints management level.[38]

[31] FSB *TCF complaints management* 1.
[32] FSB *TCF Baseline study feedback report* 0.
[33] Coleman "What is an FCA thematic review and how could it impact your firm?" 18 March 2016.
[34] FSB *TCF Baseline study feedback report* 0.
[35] FSB *TCF complaints management* 1.
[36] Treasury *Draft Market Conduct Paper* 16.
[37] FSB *TCF complaints management* 1.
[38] *Policyholder Protection Rules* 2019 chapter 8.

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The review illustrated that the needs of the customer were not being met.[39] There were inconsistencies and a non-standardized approach to dealing with customers and their complaints.[40] Customers were not able to hold their product providers accountable for their poor treatment.[41] It was recognized that there was a need to address four core issues.[42] First, the existing laws and regulations specific to complaints management practices within the insurance industry needed to be reviewed.[43] Second, the ombudsman schemes needed to be reviewed in order to ensure an efficient and affordable redress mechanism for customers.[44] This would have to be an independent, impartial, and transparent system.[45] Third, the complaints procedures within the financial institutions, and the financial literacy and capability of customers needed to be reviewed.[46] Fourth, awareness needed to be created among retail customers: they needed to be educated, made aware and informed of financial products and services, and be capable of determining whether these products and services suit their needs.[47] They needed to understand what their rights were and be aware of the steps that they could take to enforce their rights and ensure their effective and protective participation within the financial services sector.[48]

The aforementioned points of focus are still relevant today. However, whilst there is a clear need to address the fair treatment of customers within the financial services industry, there exists a need to grow and develop the industry to ensure financial stability.[49]

Through interactive engagement and reviews with the financial services industry, it was established that the fair treatment of customers is dependent on the financial services industry.[50] The plan to improve the financial stability of the financial services sector required robust regulators which focused on both aspects, in effect the financial stability of the industry as well

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[39] Treasury *Draft Market Conduct Paper* 16.
[40] FSB *TCF Baseline study feedback report* 0.
[41] FSB *TCF complaints management* 1.
[42] Treasury *Draft Market Conduct Paper* 35.
[43] *Idem* at 36.
[44] *Idem* at 57.
[45] Treasury *A safer financial sector to serve South Africa better* 10.
[46] FSB *TCF complaints management* 6.
[47] *Idem* at 1.
[48] *Ibid.*
[49] Treasury *A safer financial sector to serve South Africa better* 5.
[50] Treasury *Draft Market Conduct Paper* 16.

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as ensuring the fair treatment of customers.[51] It was this specific realisation that resulted in the adoption of the regime of Twin Peaks within the South African context for financial services.[52]

The Twin Peaks model of regulation serves both sets of needs under independent bodies as there would often be a conflict to determine which requirement should override the other.[53] This resulted in a prudential regulator and market conduct regulator, where the prudential regulator would have its focus on the financial stability of the industry, and the market conduct regulator would ensure the fair treatment of customers within the financial services industry.[54] The objective of this approach is to strengthen the industry by ensuring better customer experiences – better customer experiences are indicative of a stronger industry, in effect a broader view in terms of economic growth is taken.[55]

On 1 April 2018, South Africa announced its regulatory system change wherein two regulators were confirmed to be in operation: the Prudential Authority (PA) and the Financial Sector Conduct Authority (FSCA).[56] With this announcement, the regulatory changes of the market conduct aspects began to unfold as FSCA initiated its own strategy.[57]

2.3. An overview of the reformation of the existing regulatory structure

The 2008 global crisis highlighted how weaknesses in the financial sector can cause severe economic hardship for the man on the street.[58] Poor conduct practices played a central role in the global financial crisis. South Africa had identified shortcomings in the regulatory and supervisory frameworks which illustrated that conduct, prudential and stability risks had gone unnoticed for a lengthy period.[59] The question that thus needed to be asked was: Why did the historic structure not meet the requirements of the foreseeable change? South Africa emerged from the financial crisis with an understanding of what its protection mechanisms were which allowed its recovery.[60] These included: a sound financial regulation framework; conservative risk management practices; limited exposure to foreign assets; subsidiary structure and listing

[51] *Idem* at 63.
[52] FRRSC *Implementing a twin peaks model* 14.
[53] Treasury *Draft Market Conduct Paper* 19.
[54] Treasury *New Twin Peaks regulators established* 1.
[55] Treasury *Draft Market Conduct Paper* 19.
[56] Treasury *New Twin Peaks regulators established* 1.
[57] FSCA *Regulatory Strategy* 11.
[58] Treasury *Draft Market Conduct Paper* 85.
[59] *Ibid*.
[60] Treasury *A safer financial sector to serve South Africa better* 13.

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requirements.[61] It was further protected by strong fiscal and financial sector policies such as the monetary policy framework; countercyclical monetary policy; countercyclical fiscal policy; proactive approach to dealing with credit risks; the introduction of the National Credit Act 34 of 2005 which protected customers from reckless lending practices.[62] These were policies that served, and still serve, the purpose of strengthening and enhancing the financial stability of the country.

Nevertheless, whilst South Africa was able to recover, the consequences were far reaching. There was still a need to enhance the supervision of individual institutions, co-ordinate better and share information to enhance learnings.[63] There was a need to enhance existing capability to increase financial stability.[64] The areas which were complemented were those of financial stability in relation to institutions, whilst the impact to the financial services customer was far-reaching.[65] The support which would be rendered by strengthening financial stability was indirect in that there would be job creation, economic growth and development resulting in benefit for the customer.[66] However, there was a need to provide stability within the individual household as well as protection of financial assets and job losses.[67] It would necessitate regulation to the extent that individual households were offered products which were affordable and beneficial in times of a financial crisis.[68]

At the time of the 2008 Global Financial Crisis, the FSB was the independent body with the mandate to supervise and regulate the non-banking financial services industry, which included the insurance industry.[69] It was established in 1991 and its stated vision was "to regulate and supervise financial institutions and markets to protect consumers of financial services".[70] One of its main areas of responsibility was to ensure that there was compliance with legislation as well as capital requirements to ensure financial soundness.[71] It was endowed with enforcement powers to deal with breaches where it could impose penalties, require compensation to be paid,

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[61] *Idem* at 14.
[62] *Ibid*.
[63] *Idem* at 23.
[64] *Ibid*.
[65] *Ibid*.
[66] *Ibid*.
[67] *Ibid*.
[68] *Ibid*.
[69] FSB *2016 Annual Report* page 16.
[70] FSB *Presentation to Parliament, Strategic Plan* 3.
[71] FRRSC *Implementing a twin peaks model* 9.

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and give cost orders.[72] These orders were regarded as equivalent to a judgment of the Supreme Court of South Africa.[73] It ran a customer complaints service as well as an appeals board.[74]

Based on the outcomes of the financial crisis and the indirect consequence to financial customers, it was evident that the key focus of the FSB was, and always would be, financial stability in support of prudential requirements, as opposed to market conduct outcomes.[75] The dilemma lay in the structure of the FSB – it was based on the unified model for a regulator which attempts to address both market conduct needs and oversee the financial soundness of entities or institutions.[76] The challenge with this structure was the fact that the prudential requirements and conduct requirements required fundamentally different approaches.[77] There was also a barrier in terms of the culture and approach between the requirements and the needs of prudential and market conduct regulation.[78] There were challenges with a single regulator being unable to adequately balance this requirement.[79] A further challenge was the fact that a single regulator did not provide the necessary focus on the varying objectives and rationale of regulation and supervision.[80] A single regulator was only able to differentiate between the different types of institutions and their holistic needs, as opposed to the specific elements of prudential versus market conduct regulation.[81]

As noted above, it is clear that the key focus was on the prudential requirements supporting and strengthening financial stability. The market conduct risks received attention, however to a lesser extent.

The FSB had initially focused on being a prudential regulator within the non-banking financial sector.[82] However, over a period, it expanded its role to include the issues of customer protection.[83] The FSB was unfortunately not able to mitigate several incidents within the insurance sector.[84] A few areas of concern which arose were the need to balance the conflict

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[72] *Idem* at 12.
[73] Kruger *FSB Enforcement Committee* 30 July 2013.
[74] FSCA *Regulatory Strategy* 14.
[75] FSCA *Regulatory Strategy* 14.
[76] FSCA *Regulatory Strategy*, 14.
[77] Treasury *Draft Market Conduct Paper* 85.
[78] *Ibid*.
[79] FSCA *Regulatory Strategy* 14.
[80] Treasury *Draft Market Conduct Paper* 85.
[81] Godwin (2017) “Australia’s Trek toward Twin Peaks – comparisons with South Africa”, *Law and Financial Markets Review* 151-153.
[82] FSB *Presentation to Parliament, Strategic Plan* 8
[83] *Idem* at 7.
[84] Treasury *Draft Market Conduct Paper* 85.

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between financial stability, consumer protection, competitiveness, and affordability.[85] Market conduct risks had gone unnoticed for some time and this was an obvious shortcoming in the regulatory and supervisory framework,[86] due to the split focus of its responsibilities.[87]

The objectives of the Financial Sector Regulation Act[88] (FSRA) sets out the responsibilities of the regulators relating to financial stability and market conduct as it would apply to financial institutions. The responsibility for micro-prudential regulation in respect of financial stability will now rest with the PA.[89] The FSRA also sets out the responsibilities relating to the protection of customers.[90] These responsibilities relate to financial institutions and the Regulator is intended to manage and supervise the manner in which financial institutions treat their customers. This aspect will be managed by the FSCA.[91] These responsibilities previously rested with the FSB, and one would appreciate that there was a conflict regarding how to balance the needs of the customer against the financial stability needs of the insurance industry.[92]

In respect of content-based market conduct regulation, the FSB was responsible for the implementation of the TCF approach in South Africa. Its purpose was to design a programme for the regulation of financial services institutions specific to how they treated their customers.[93] The programme comprised of six fairness outcomes in respect of which financial institutions would be expected to demonstrate achievement of same for their customers.[94] These fairness outcomes existed throughout the value chain of the service offering, meaning from product discussions up to and including the complaint management process.[95] This approach supported the minimum and necessary elements for an effective market conduct framework, i.e. a strong legal and regulatory regime which had customers and fair outcomes at its epicentre, well-known and functioning complaint mechanisms, and mindful, knowledgeable financial customers as a result of training and development.[96]

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[85] FRRSC *Implementing a twin peaks model* 28.
[86] Treasury *Draft Market Conduct Paper* 85.
[87] FSB *Twin Peaks Newsletter* Issue 1.
[88] 9 of 2017.
[89] FSB *Twin Peaks Newsletter* Issue 2.
[90] *Ibid.*
[91] *Ibid.*
[92] FRRSC *Implementing a twin peaks model* 9.
[93] FSB *TCF Road Map* 18.
[94] FSB *TCF complaints management* 10.
[95] FSB *TCF Roadmap* 3.
[96] Treasury *Draft Market Conduct Paper* 85.

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The challenge which the Regulator is faced with is that, generally, the financial services industry is dominated by the larger financial institutions.[97] These institutions therefore set the scene for a typical customer base and the small number of dominant financial institutions reduce the ability for competitiveness within the market.[98] Due to the dominance factor, these financial institutions often dictate the features of the product, which is usually complex with specific fee structures and the pricing is therefore higher than it would be if there had been a greater number of institutions offering the product.[99] The offerings are also limited to a specific group of South Africans and therefore not accessible to all customers.[100] Therefore, the wealthier, urban customers have access to a variety of products or services compared to the average South African who only has access to a limited range of products that may not even be suitable to his or her specific needs.[101] The latter group of customers may receive no product at all due to the costs resulting in the product being inaccessible to them.[102]

The insurance industry offers products which range from simple to complex. Generally, the more complex a product or offering, the greater the risk of unfair treatment of the customer due to customers not being financially savvy.[103] This warrants greater regulatory protection. A financial sector that conducts itself with integrity, in the interests of real customer needs, promotes confidence in the sector by delivering better outcomes for customers and the economy.[104] Customers should believe that they can save, transact, borrow, and invest their funds in the financial sector and, by doing so, contribute to the growth and strengthening of the economy.[105] Poor conduct practices compromise customer and economic outcomes, inhibiting growth, trust and confidence in the sector.[106] The link between how the financial sector treats customers and South Africa's economic health, warrants governmental attention to the manner in which the sector behaves.[107] This necessitated interventions, which included regulatory changes to minimize potential customer abuse and to optimize customer value.[108]

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[97] Treasury *Explanatory policy paper accompanying COFI* 5.
[98] *Ibid.*
[99] *Ibid.*
[100] *Ibid.*
[101] *Ibid.*
[102] *Ibid.*
[103] Treasury *Draft Market Conduct Paper* 85.
[104] *Idem* at 86.
[105] *Ibid*.
[106] *Ibid*.
[107] *Idem* at 85.
[108] *Idem* at 86.

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The Twin peaks reform was therefore an important opportunity to reform South Africa's market conduct regulatory framework.[109] The FSRA will be complemented by market conduct legislation to ensure that the regulator is adequately equipped with the tools to satisfy its mandated functions and responsibilities.[110] The market conduct legislation which is intended to complement the FSRA is the Conduct of Financial Institutions Bill (COFI). Its aim is to strengthen the legislative framework for the manner in which the financial services industry treats its customers.[111] The FSRA currently provides for the functions and powers of the FSCA. COFI will provide the substantive detail relating to what consumers can expect of financial institutions.[112] The Bill has an outcomes-based focus, in respect of which a supervisory body will be in a position to test a financial institution's ability to deliver on real outcomes.[113]

In a similar fashion, the FSRA requires that the FSCA effects its duties in the form of outcomes-based supervision.[114] The FSCA's focus is therefore on customer outcomes as opposed to determining whether institutions are merely following a compliance checklist.[115] In order to create a financial sector that works in the interest of the customer, the FSCA will have to scrutinize the relationship between a financial institution and its customer.[116]

The outcomes-based approach aims to test financial institutions on their delivery of the TCF outcomes, or on their pricing efficiency, or their transparency.[117] This would relate to conduct of business and market integrity objectives.[118] The approach allows for adherence from the perspective of aligned regulatory frameworks which are robust and adequate to capture all activities that impact on the integrity of the market and to ensure fair outcomes to its customer base.[119] It prevents arbitrage between requirements which are not the same.[120] The focus of the outcomes-based supervisory approach would be on financial sector policy outcomes and testing the sector's effectiveness in supporting the South African economy.[121] For example,

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[109] Treasury *Draft Market Conduct Paper* 24.
[110] Treasury "Invitation for public comments on the draft COFI Bill 2018" 11 December 2018.
[111] *Ibid.*
[112] *Ibid.*
[113] *Ibid.*
[114] FSCA *Regulatory Strategy* 54.
[115] *Ibid.*
[116] *Idem* at 16.
[117] Treasury *Draft Market Conduct Paper* 86.
[118] *Ibid.*
[119] *Ibid.*
[120] FSCA *Regulatory Strategy* 54.
[121] Treasury *Draft Market Conduct Paper* 87.

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the Regulator would be expected to consider whether the market and regulatory structures are supporting the average South African in saving enough to meet his/her/its needs over short, medium- and long-term financial goals.[122] Where an enquiry reveals a potential problem, the Regulator would be expected to analyse the reasons for the problem, specifically those related to regulated entities or the supporting regulatory environment.[123]

2.4. The regulatory and legislative reforms to the financial sector in South Africa

2.4.1. Orientation

In February 2011, South Africa committed to a safer financial sector.[124] Reforms relating to the financial sector were initiated and one of the core aspects was the commitment to improve the regulatory structures that support financial regulation.[125] The reforms were officially implemented, albeit in phases, from 2018 onwards.

The FSRA empowers and increases the FSCA's ability to improve conditions, and provide protection, for customers where there is poor conduct or behavior from financial institutions; overcome adverse conditions; and enhance financial stability and financial sector integrity.[126] The legislation aims to ensure that the FSCA is able to monitor and supervise the manner in which financial institutions conduct business to ensure the fair treatment of customers.[127] The FSRA mandates the PA to supervise the safety and financial soundness of financial institutions.[128] Section 58(1)(c) of the FSRA determines that the FSCA must work with the PA as provided for in the legislation.

As indicated above, the FSCA has four primary objectives of equal importance.[129] It must: first, enhance the efficiency and integrity of financial markets; second, promote fair customer treatment by financial institutions; third, provide financial education and promote financial literacy; and four, assist in maintaining financial stability.[130] Following this, there is an expectation from the customer base of the financial industry that the new regulatory

[122] Treasury *A safer financial sector to serve South Africa better* 6.
[123] Treasury *Draft Market Conduct Paper* 36.
[124] FSB *TCF Road Map* 36.
[125] FRRSC *Implementing a twin peaks model* 2.
[126] FSB *Twin Peaks Newsletter* Issue 2.
[127] *Ibid*.
[128] *Ibid*.
[129] FSCA *Regulatory Strategy* 10.
[130] Section 57 of the FSRA.

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framework will lead to more appropriate products and services.[131] Financial customers expect that products and services will be sold in a more transparent manner, with better accountability by financial institutions.[132]

As the focus of this dissertation is on the FSCA and how complaints management would evolve to enhance market conduct practices within the insurance industry in a South African context, the expectation from the consumer base relevant to this discussion is that financial institutions will review and analyse feedback from submitted complaints in order to understand the needs of the customer base.[133] The FSCA's intention is to adopt a proactive approach where risks are pre-empted. A practical step to effect this principled approach is the following: A qualitative and quantitative analysis of complaints should be done for purposes of training and coaching a financial institution's staff or as a tool to establish process and product improvements.[134] This would allow a financial institution will to identify and mitigate risks within its organization.[135] From the Regulator's perspective, the data can be utilized to identify trends for purposes of mitigating risk or to confirm the success, progress, and failures of an initiative.[136] An analysis of trends relating to the complaints of financial institutions is a source of such data and sources such as ombud schemes, social media, and other reporting mechanisms may be utilized.[137] The question that arises, and which is dealt with in an upcoming chapter, is whether the means to properly achieve the above are in place or whether there is a discrepancy between the laudable outcomes and the mechanisms to effect these outcomes.

2.4.2. Regulatory reform

The FSCA's powers, as conferred upon it by the FSRA, provide a toolkit for it to perform its functions. The FSCA's focus remains on regulating and supervising financial institutions with a specific focus on delivering fair customer outcomes.[138] Its responsibility in terms of regulation nevertheless extends further than the entity itself – it extends to cover aspects of

[131] FSCA *Regulatory Strategy* 30.
[132] *Ibid.*
[133] FSB *TCF Complaints Management* 9.
[134] *Ibid.*
[135] FSCA *Regulatory Strategy* 53.
[136] FSB *TCF Complaints Management* 9.
[137] FSCA *Regulatory Strategy* 53.
[138] Section 131 to 144 of the FSRA.

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the conduct of key persons and control functions of financial institutions, its representatives, and outsourcing arrangements entered into by financial institutions.[139]

In order to regulate the industry, the FSCA has the power to make conduct standards and joint standards with the PA under the FSRA, in addition to any powers conferred on it under sector-specific laws.[140] The FSRA makes provision for the FSCA to set these standards for financial services providers.[141] The authority given in respect of this rule making instrument for conduct standards enables the FSCA to give effect to the powers bestowed upon it: "In effect, conduct standards are the rule-making instrument created through the FSR Bill to give effect to legislative powers delegated to the FSCA i.e. they will apply generally to the industry, sub-sector or category of financial institution or regulated activity concerned."[142] In the context of complaints management, section 106(3)(c)(iii) allows the FSCA to issue conduct standards in respect of "requirements for the fair treatment of financial customers, including in relation to … the resolution of complaints and disputes concerning those products and services, including redress".

Regarding the FSCA's ability to offer guidance to the financial sector, sections 141 and 142 determine that the Regulator may issue non-binding, explanatory "guidance notices" regarding financial sector laws; as well as "interpretation rulings". In respect of interpretation rulings, section 142(2) determines that "[t]he purpose of an interpretation ruling is to promote clarity, consistency and certainty in the interpretation and application of financial sector laws" and is generally in force until the law is amended or the Regulator's determination changed by a court of law.[143]

As part of its information gathering authority, the FSCA may request information or documents in writing from the sector should there be a view that there is a breach of a financial sector law.[144] The regulated entity (for purposes of this dissertation, it would be the insurance company) must comply with the request for information.[145] The FSCA may utilize mystery shopping as an avenue to gather information.[146] The Regulator may request an on-site visit

[139] FSCA *Regulatory Strategy* 13.
[140] Section 106 of the FSRA.
[141] Section 106(1)(a) of the FSRA.
[142] Treasury *Draft Market Conduct Paper* 37.
[143] Section 142(4) of the FSRA.
[144] Section 131 of the FSRA.
[145] *Ibid.*
[146] FSCA *Regulatory Strategy* 41.

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(also referred to as "supervisory on-site visits") for purposes of checking compliance with financial sector laws to determine risks posed by potential contravention of financial sector laws.[147] In respect of its ability to conduct investigations, the FSCA may instruct an investigator to be appointed in the event that there is suspicion that a financial sector law is being contravened or there is a reasonable belief that an investigation is required for the FSCA to meet its objectives.[148]

Non-compliance confirmed by the Regulator may have the following implications, which are also applicable to the insurance industry and complaints management. The FSCA has several remedial avenues available to it, depending on the reaction or manner in which the financial institution or individual responds. The FSCA may enter into an enforceable undertaking with an individual or institution where the individual or institution is in agreement to effect remedial action following a regulatory contravention.[149] The purpose of this agreement is to improve efficiencies within the financial institution.[150] There would be co-operation from the financial institution to remedy the failure in terms of conduct.[151] Should there be a failure to comply with the enforceable undertaking, same would constitute a failure in terms of the law and would likely result in the Regulator taking action.[152]

Where there is an issue with how the financial institution conducts its business, the FSCA may issue a directive, and the financial institution would be required to take specific action to remedy the situation.[153] The FSCA will intervene where it has noted significant misconduct, or abuse and widespread prejudice to multiple customers.[154] The authority is awarded to the FSCA to issue directives to financial institutions to remedy the effects of the financial institution's contravention of the law.[155] The financial institution may be required to provide redress to its customers that were impacted.[156]

[147] Section 132 of the FSRA.
[148] FSCA *Regulatory Strategy* 57.
[149] *Ibid*.
[150] *Ibid*.
[151] *Ibid*.
[152] FSCA *Regulatory Strategy* 57.
[153] Section 144 of the FSRA.
[154] Section 144 of the FSRA.
[155] Section 144(3) of the FSRA.
[156] Section 144(3) of the FSRA.

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2.4.3. Discussion

The question that arises in relation to the need for change in terms of the existing regulatory structure is thus: Why did the historic structure not meet the requirements of the foreseeable change?

First, the Twin Peaks regulation recognizes that the two objectives – that of financial soundness and treating customers fairly – have better value if a separate regulator is allocated to each function.[157] The Global Crisis of 2008 highlighted that the financial services sector is a very real part of the South African economy in that the financial services sector touches the life of each individual.[158] The financial services sector enables daily transacting, savings, preservation of wealth, retirement and insuring against disasters.[159] From a macroeconomic standpoint, the financial sector allows for economic growth, job creation and the building of an infrastructure.[160] With that realization, the crisis highlighted that the financial institutions were in a position to survive the crisis due to their resilience, however the indirect impact on consumers demonstrated that there was a gap in regulation.[161] The indirect impact were the loss of employment, which had a devastating impact. This highlighted the fact that the financial services sector was poorly regulated when it came to consumer welfare.[162]

While there is a need to ensure the continued maintenance of a robust financial services sector, the sector should also be in a position to provide financial services to a market where there is an absolute need for quality products. These products ought to be available at an affordable rate and suit the needs of the customers.[163] It was therefore of importance to understand that there were different needs and each required ongoing regulation, monitoring, and supervision to ensure financial stability; customer protection and market conduct; expansion through financial inclusion and the combatting of financial crime.[164] Historically, these functions were performed by the FSB but have now been divided amongst the PA and FSCA (and some other bodies such as the Financial Intelligence Center).[165]

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[157] FRSC *Implementing a twin peaks model* 3.
[158] Treasury *A safer financial sector to serve South Africa better* 1.
[159] *Ibid.*
[160] *Ibid.*
[161] *Ibid.*
[162] Treasury *A safer financial sector to serve South Africa better* 1.
[163] *Ibid.*
[164] *Idem* at 4.
[165] *Idem* at 23.

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Second, the mandate of the FSCA confirms an outcomes-based[166] and risk-based approach to supervision.[167] The new approach seeks to change behaviour to effect better outcomes for customers.[168] The FSCA intends to adopt a judgment-style approach wherein the supervision procedure involves the interrogation of a financial institution and its strategy.[169] In order to understand and challenge a financial institution on its conduct, the FSCA requires insight into an organization's culture and its key themes in respect of the driving-force behind the behaviour of the financial institution when making certain decisions.[170]

The approach would be supervisory, where outcomes to customers would be monitored.[171] It is a requirement for the FSCA to monitor whether the financial institution is delivering fair and appropriate financial products and financial services to its customer base.[172] Its purpose is for the industry to include fair practices in terms of TCF throughout its product life cycle.[173] This means that at every step of its development of product and service thereof, a firm should consider the outcome for its customer.[174] The approach of the Regulator would be to supervise and support the firm, where required,[175] and its regulatory strategy is to engage with financial institutions in open and transparent consultation processes when making regulatory decisions.[176] Financial institutions know and understand their business and they would therefore be better placed to determine the processes and actions which their businesses would require to achieve the desired outcomes.[177] Financial institutions would be required to satisfy the Regulator that they have effective governance processes in place to support the delivery of such outcomes.[178]

However, for this supervisory approach to be effective, it must be structured in such a manner that, where financial institutions pose a greater risk of unfair treatment to their customers, they are subjected to a more intrusive and intensive supervision than those who pose a lower market conduct risk.[179] Greater oversight and additional capability on the part of the FSCA will be

[166] FRRSC *Implementing a twin peaks model* 45.
[167] FSCA *Regulatory Strategy* 53.
[168] *Idem* at 54.
[169] *Idem* at 54.
[170] FSCA *Regulatory Strategy* 54.
[171] *Ibid.*
[172] Section 58(1)(i) of the FSRA.
[173] FSCA *Regulatory Strategy* 54.
[174] Treasury *Draft Market Conduct Paper* 16.
[175] FSCA *Regulatory Strategy* 54.
[176] Section 70(2) of the FSRA.
[177] Ernst & Young *Financial Sector Regulation Act, implementing twin peaks and the impact on the industry* 13.
[178] Treasury *Explanatory policy paper accompanying COFI* 10.
[179] FSCA *Regulatory Strategy* 54.

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required to monitor and communicate trends relating to conduct risks, whether existing or emerging, to the industry.[180]

In essence, FSCA's purpose will be to protect customers of financial service providers from unfair treatment and to ensure the promotion of confidence in the South African financial system.[181] Unlike the FSB, it is not intended to be a body which handles complaints received from customers, unless the complaint relates to a contravention of a financial sector law.[182] The FSCA does not deal with complaints from customers which relate to service delivery or disputes relating to the outcome of a claim. There are various ombud schemes which are mandated to monitor and deal with these complaints through a fair and impartial process.[183] The FSCA will work with the various ombud schemes to understand the trends and types of complaints which they receive – for regulatory purposes and to meet its own statutory objectives.[184] In turn, the ombud schemes work with the FSCA and refer matters where a contravention of a financial sector law is noted or where it is determined that financial institutions illustrate a trend relating to poor outcomes for customers.[185]

The above discussions dealt with the regulatory framework that forms the foundation for complaints management in South Africa. However, complaints management also functions within a specific substantive legislative arena, which is dealt with next. Aspects relating to the ombud schemes are dealt with in chapter four.

2.4.4. Legislative reform

Through the years, a range of laws were introduced within the sector to improve practices which impact conduct. The laws which had its focus on conduct of business were numerous and operated in silos. Financial institutions were therefore subject to inconsistent legal frameworks relating to market conduct which created an opportunity for regulatory arbitrage.[186] The laws, specific to the insurance industry and which impacted conduct under specific categories of the product cycle comprised of: the Long-Term Insurance Act[187] (which deals with governance, issuing of products, sales and distribution, disclosures, post-sale service

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[180] *Idem* at 28.
[181] *Idem* at 29.
[182] *Idem* at 18.
[183] *Idem* at 16.
[184] *Ibid.*
[185] *Ibid.*
[186] Treasury *Draft Market Conduct Paper* 16.
[187] 52 of 1998

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and claims); the Short Term Insurance Act[188] (which deals with governance, issuing of products, sales and distribution, disclosures, post-sale service and claims); the Financial Advisory and Intermediary Services Act[189] (FAIS Act, which regulates sales and distribution, specific to intermediary services, advice, disclosure (on intermediated business), post-sale service (on-going advice) and complaints specific to advice or intermediary services); and the Financial Services Ombud Schemes Act[190] (FSOS Act, which regulates complaints resolution).[191]

The future framework will comprise of the FSRA and, potentially, only COFI.[192] Until all the laws are repealed as part of the implementation of COFI, these laws remain applicable – for example, currently, the General Code of Conduct under the FAIS Act also forms part of the pre-Twin Peaks legislation still in operation.[193] The intention is to incorporate some of these definitions and practices into the market conduct regulatory framework with a view to ensure alignment under Twin Peaks and COFI.[194]

The intention of the revision is twofold: first, to strengthen the legislative conduct framework and, second, to streamline the conduct requirements and to bring same into fewer legislative frameworks.[195] The purpose of this market conduct reformation process is to support regulatory changes to ensure the delivery of the TCF outcomes within regulatory frameworks until the promulgation of the COFI.[196] This would ensure that, when the COFI comes into force, the existing structures and frameworks could transition into the standards under the COFI.[197] The TCF outcomes are therefore constantly referenced as the guiding principles for rules and frameworks, specifically where the products of financial institutions have a direct or indirect impact on retail customers.[198]

As indicated above, several laws were introduced into the legislative framework governing the insurance sector with the aim of improving market conduct. This resulted in a number of changes to insurance practices. The PPRs, which were first introduced in 2001, were reviewed

[188] 53 of 1998
[189] 37 of 2002.
[190] 37 of 2004.
[191] Treasury *Draft Market Conduct Paper* 15.
[192] *Idem* at 34.
[193] *Ibid*.
[194] *Ibid*.
[195] *Ibid*.
[196] *Ibid*.
[197] *Ibid*.
[198] FSCA *Regulatory Strategy* 38.

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and enhanced in 2011 to set clear rules relating to the repudiation of claims by insurers.[199] Same also extended to clarify the time limitations and disclosures by insurers relating to legal proceedings by policyholders against insurers.[200] In 2014, the PPRs were extended to incorporate the principles of TCF.[201] It is clear that these developments occurred prior to the implementation of the Twin Peaks model of regulation in South Africa, although much of the developments occurred parallel to the conceptualisation and design of the Twin Peaks model.

COFI constitutes post-Twin Peaks legislative reformation. It will extend the scope of the FSCA's jurisdiction and amend the FSRA.[202] The proposed legislation is intended to replace conduct provisions in existing financial sector laws and aims to build consistent, strong, and effective market conduct legislative frameworks for all financial services institutions.[203] The FSRA will thus regulate the FSCA, and COFI will determine what customers may expect of financial institutions.[204] The enactment of COFI would likely warrant an amendment to the FSRA from the perspective of alignment. As discussed above, the FSRA provides the FSCA with the mandate to set standards, but COFI aims to provide the detail on what these standards should be.[205]

COFI is intended to be the creation of a single law regulating market conduct for all financial institutions.[206] It aims to replace conduct provisions in existing financial sector laws as well as build consistency and effectiveness in the market conduct framework which regulates all institutions performing financial activities.[207]

In keeping with the themes of TCF, COFI has been informed by these outcomes.[208] COFI's design is set out to be activity-, principles- and outcomes-based – the draft Bill encompasses principal requirements in law which allows the FSCA to establish monitoring principles and enforcement action where necessary.[209] The intention of this approach is to focus the attention of the Regulator on reducing the risk of barriers and ensuring that it is able to achieve its goal

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199 FSCA *Proposed amendments to the PPR Consultation Report* 11.
200 *Idem* at 71.
201 *Idem* at 121.
202 Ernst & Young *Financial Sector Regulation Act, implementing twin peaks and the impact on the industry* 5.
203 Treasury *Explanatory policy paper accompanying COFI* 4.
204 *Idem* at 21.
205 *Ibid.*
206 *Idem* at 11.
207 *Idem* at 4.
208 *Idem* at 11.
209 *Ibid*.

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of transformation.[210] The principles-based approach moves away from rules and places a focus on setting standards for the manner in which a financial institution should run its business.[211] It supports inclusion – the objective of COFI is to support financial inclusion in order to protect customers within the sector.[212] It also supports competition and innovation.[213] As previously indicated the FSRA is regulator facing, in effect intended to provide the Regulator with the guidance on how to regulate financial institutions, and confirming what customers and financial institutions can expect of the Regulator.[214] The COFI Bill provides customers and financial institutions an overview of what is expected of financial institutions.[215] Amendments to the FSRA will likely become a reality once COFI is enacted. This will be for purposes of aligning the regulations.[216]

Principles arising out of the 2014 discussion document were taken into account when drafting the COFI Bill.[217] First, the approach is activity-based.[218] There are thirteen financial sector laws which governed financial institutions. These laws regulate and supervise an institution based on their definition.[219] The new framework creates a shift away from the silo approach and moves toward an activity-based approach, meaning that the COFI Bill will define the activities undertaken in the financial sector.[220] Therefore, regardless of the activities being performed by an institution, it will be regulated and governed in the same manner.[221] This will allow for consistency from a regulatory and substantive legislative perspective.[222]

Second, the legislation is principles-based.[223] Historically, the regulator's focus was on technical compliance with the law because the legislation set out rules that could be complied with in a "tick-box" fashion.[224] COFI creates a shift from the narrow rigid focus on rules toward ensuring the spirit of the law is highlighted by incorporating outcomes and principles into the legislation.[225] A principles-based approach seeks to set principles that specify the intention of

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[210] *Idem* at 12.
[211] *Ibid*.
[212] *Idem* at 11.
[213] *Ibid*.
[214] *Ibid*.
[215] *Idem* at 21.
[216] *Ibid*.
[217] *Idem* at 11.
[218] *Ibid*.
[219] *Ibid*.
[220] *Ibid*.
[221] *Ibid*.
[222] *Ibid*.
[223] *Ibid*.
[224] *Ibid*.
[225] *Ibid*.

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regulation, rather than set rules detailing requirements of a financial institution.[226] It is important that the rules still exist, however, a balance is to be created to achieve desired outcomes.[227]

Third, in line with an outcomes-focused perspective, the conduct policy framework is intended to support the delivery of policy outcomes; allow for monitoring to ensure the outcomes are achieved; allow for preventative action to be taken where the outcomes are not being achieved and for remedial action to be taken when poor outcomes are identified.[228]

As an interjection, it is important to note that the above was, and possibly still is, not a reality in South Africa. The compliance process encompassed visits by the regulator to check compliance requirements in accordance with the law.[229] The identification and remediation of poor outcomes was/is an inefficient process.[230] The new approach relating to an evaluation of market conduct of financial institutions should ideally focus on whether financial institutions are conducting themselves in a manner which delivers the desired outcomes for customers.[231]

Fourth, a proportional approach is required to allow the FSCA to apply different levels of risk arising from different types of risk which arises.[232] The new framework is expected to enable the FSCA to identify those areas that pose the greater market conduct risk and use the appropriate capacity to address these risks.[233] Chapter 1 (clause 7) of COFI sets out guidelines for what the FSCA should consider when applying the proportionate approach.[234]

TCF remains a core indicator of acceptable market conduct behaviour. It is embedded in financial sector regulation[235] as a regulatory and supervisory approach that seeks to ensure that financial institutions, including insurers, demonstrate and deliver clearly articulated fairness outcomes for financial services customers, such as insurance clients, throughout the typical financial product lifecycle.[236]

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[226] *Ibid*.
[227] *Ibid*.
[228] *Ibid*.
[229] *Ibid*.
[230] *Ibid*.
[231] *Ibid*.
[232] *Ibid*.
[233] *Idem* at 12.
[234] *Idem* at 12.
[235] Millard and Maholo (2016) "Treating Customers Fairly: A New Name for Existing Principles" *THRHR* 594.
[236] FSCA *Regulatory Strategy* 37.

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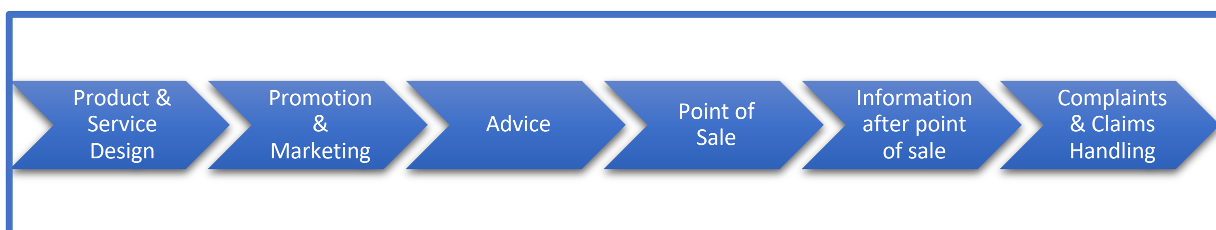
The TCF outcomes articulate the manner in which the FSCA expects financial institutions to deal with their customers.[237] The FSRA included the TCF approach in its framework by providing the FSCA with an explicit directive of promoting the fair treatment of financial customers and empowering it to make conduct standards that were aimed at ensuring that this directive was met.[238] COFI aims to further incorporate these principles, and its focus will be on retail customers.[239] Although COFI has a principles-based focus – meaning that it does not set out specific rules, but rather the intention of the rules[240] – it will still function alongside the FSCA's conduct standards that will be developed to ensure delivery of the six TCF outcomes.[241] The FSCA's intention is to adopt an incremental approach to working towards an overarching conduct of business framework that promotes the TCF outcomes.[242] The approach embeds TCF in the existing regulatory, supervisory and enforcement frameworks and continues to prioritise several key TCF aligned regulatory projects.[243]

The approach seeks to ensure fairness outcomes for customers delivered by an adequately regulated industry.[244] It further intends to incorporate customer confidence by ensuring the supply of appropriate financial products and services through enhanced transparency and discipline.[245] TCF is to ensure that financial institutions consider the fair treatment of customers throughout the product lifecycle.[246] Financial institutions would be expected to demonstrate this through monitoring and management behaviours.[247] TCF's fairness outcomes apply to all the stages of a typical product life cycle. An illustration would be:[248]



[237] FSB *CBR's Response to industry comments* 2.
[238] Sections 57 and 106 of the FSRA.
[239] Department Planning, Monitoring & Evaluation *Initial impact of COFI* 7.
[240] Treasury *Explanatory policy paper accompanying COFI* 11.
[241] *Ibid.*
[242] Department Planning, Monitoring & Evaluation *Initial impact of COFI* 18.
[243] Treasury *Explanatory policy paper accompanying COFI* 14.
[244] FSB *TCF complaints management* 20.
[245] *Ibid.*
[246] *Ibid.*
[247] FSB *TCF Road Map* 8.
[248] *Idem* at 9.

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There are six targeted outcomes.[249] The first outcome is that customers are confident that they are dealing with financial institutions for whom the fair treatment of customers is central to their culture.[250] This basically means that the core function of a financial institution has fair customer outcomes at the center of its strategy. The second outcome is that products and services marketed and sold in the retail market are designed to meet the needs of the identified customer groups, the features of the product or service are fair and adequate, and not confusing and overly complex in relation to the customer base to which it is sold.[251] The third outcome is aimed at ensuring that customers are given clear information and are kept appropriately informed before, during, and after the time of contracting.[252] This links with the fourth outcome, in that where customers receive advice, the advice is suitable and takes account of their circumstances.[253] The fifth outcome focuses on ensuring that customers are provided with products that perform as financial institutions have led them to expect, and the associated service is both of an acceptable standard and what they have been led to expect.[254] The sixth outcome is that customers do not face unreasonable post-sale barriers to change products, switch providers, submit a claim or make a complaint.[255] This outcome is aimed at ensuring that financial institutions have a simple process allowing customers to change or switch products or lodge a claim or complaint.

The TCF regulatory framework aims to achieve a number of high-level policy outcomes:

- Consistency: The consistency outcome will be in relation to delivering of fair outcomes to customers;
- Completeness: This is to ensure that existing regulations do not present obstacles to the fairness outcomes – the framework is intended to close any gaps within existing customer protection initiatives;
- Co-ordination: The framework will require co-ordination with all legislation to prevent duplication; and
- Alignment with international best practice: In the event of any inconsistencies or contradictions in South African principles, international standards will apply.[256]

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[249] FSB *TCF complaints management* 10 – 14.
[250] *Idem* at 11.
[251] *Ibid*.
[252] *Idem* at 12.
[253] *Ibid*.
[254] *Ibid*.
[255] *Idem* at 13.
[256] FSB *TCF Roadmap* 16.

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The TCF Roadmap was published shortly after the announcement of the Twin Peaks model, which highlighted TCF as an important component to strengthen the market conduct objectives of the financial sector.[257] The Roadmap illustrated that it would be useful to have an initial picture of how customers were being treated and how financial institutions would measure against the six outcomes.[258] This would provide a benchmark for future assessments against the delivery of the TCF outcomes.[259]

As such, reporting requirements on TCF now form part of the quarterly reporting duties of financial institutions – reporting to the FSCA – in terms of Conduct of Business Returns (CBRs).[260] The rationale for including these requirements and the categorization of complaints is to assist the financial institution and the FSCA to identify trends, root causes for complaints, and areas for improvement relating to products sold or services rendered.[261] The CBRs are reviewed and improved on an ongoing basis.

TCF outcome six requires a more consistent and comprehensive regulatory framework for complaints management.[262] The FSCA's role is to strengthen the complaints management regulatory requirements and align standards across the sectors.[263] Gaining insight into complaints management within the financial institutions will support the oversight and supervisory aims of the FSCA.[264] There will be an expectation for financial institutions to demonstrate to the FSCA how they are using their complaints management processes and data to identify and remedy poor customer outcomes.[265] Complaints data from financial institutions and ombudsman schemes assist in tracking and monitoring trends to effect corrective action where poor customer outcomes are identified.[266]

2.4.5. Discussion

TCF is regarded as a "framework for tougher market conduct oversight" which is intended to optimize processes and the manner in which financial institutions treat their customers.[267] The

[257] FSB *Road Map* 6.
[258] *Idem* at 11.
[259] FSB *Baseline Report* 11.
[260] FSB *CBR's Response to industry comments* 2.
[261] *Ibid.*
[262] *Policyholder Protection Rules* 2019 chapter 8.
[263] *Ibid*.
[264] FSB *CBR's Revised Categorisation, questions and reporting levels* 2.
[265] *Ibid*.
[266] FSCA *Regulatory Strategy 2018 to September 2021* 38.
[267] *Idem* at 14.

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TCF program is intended to be the foundation for the enhanced market conduct regulatory approach.[268] Rules and regulations will have to be clear, enforceable and fair in order for the implementation of the TCF framework to be effective.[269] Past experience has indicated that financial institutions cannot be expected to "do the right thing" out of their own accord.[270] A regulatory framework will therefore have to be established which will effectively balance the principles-based and rules-based regulation to ensure that firms deliver, and are able to deliver, in terms of the expected outcomes.[271]

It is expected that the regulatory framework will consist of legislation, subordinate legislation, and specific guidance enabling financial institutions to understand the expectations of the FSCA.[272] Financial institutions are expected to develop processes and controls to ensure adherence to the rules-based components of TCF.[273]

In the sphere of legislative reform, change has been effected through a number of interventions. The first intervention was in relation to the laws governing the financial sector in order to align these with the TCF outcomes.[274] Upon completion of the analysis on alignment, a set of regulatory amendment recommendations had to be developed for each theme.[275] The regulatory framework would then have to be finalized: once engagements and consultations had been finalized, the normal legal process would be followed to reach finality.[276] As such, this is an ongoing process with room to highlight shortcomings and recommend reformative action.

Closely related to regulatory alignment, is regulatory co-ordination because co-ordination between regulators is a key feature of the financial regulatory framework.[277] This is not only relevant for the FSRA, because COFI also recognizes that the PA and FSCA operate alongside each other.[278] A typical example would be where areas of duplication in the law exist – here the Regulators would be expected to work together to resolve this with minimal disruption.[279]

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[268] FSB *TCF Road Map* 12.
[269] *Ibid*.
[270] *Ibid*.
[271] *Ibid*.
[272] *Ibid*.
[273] *Policyholder Protection Rules* 2019 chapter 8.
[274] FSB *TCF Road Map* 18.
[275] *Ibid*.
[276] *Ibid*.
[277] *Ibid*.
[278] Treasury *Explanatory policy paper accompanying COFI* 21.
[279] *Idem* at 22.

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From an insurance perspective, it is trite that these institutions pose prudential as well as market conduct risks.

A contemporary legal framework would be inefficient without a well-developed supervisory framework. In order for the supervision to be effective, a number of requirements must be incorporated into the system.[280] The supervision must be structured to ensure that financial institutions posing a higher risk of customer dissatisfaction should be subject to a more intensive supervision than those posing a lower risk.[281] This is known as "risk-based and proportional" supervision.[282] The approach by the FSCA and its supervision will be affected by proportionality, meaning that those institutions who are identified as a lower risk will receive less intrusive supervision.[283] In relation to supervision that is "proactive and pre-emptive", the Regulator will be required to build additional capacity to monitor trends relating to conduct risk.[284] Oversight of financial institutions will have to be more intrusive and extensive.[285]

The FSCA has indicated that it intends to be proactive as opposed to reactive, and that it should be in a position to identify areas of concern or potential failures as opposed to identifying these through complaints illustrating that the customer has already suffered some loss or been prejudiced.[286] In order for the FSCA to be clear, fair and transparent in its processes, it will require greater insight into a financial institution having embedded TCF.[287] The only manner of ensuring this is to have more stringent supervision over financial institutions and demand greater detail from a reporting perspective in order to determine whether intervention is needed.[288] Once a risk is identified, detailed engagement with a firm must take place to prevent potential harm to consumers and continuing conduct failures.[289]

Complaints management reporting has been under review in order to align practices with TCF categorization and compliance reporting.[290] The TCF Roadmap provided an indication of

[280] Treasury *Draft Market Conduct Paper* 5.
[281] *Ibid*.
[282] *Ibid*.
[283] *Ibid*.
[284] *Ibid*.
[285] *Ibid*.
[286] FSB *TCF Road Map* 22.
[287] *Ibid*.
[288] *Ibid*.
[289] *Ibid*.
[290] *Ibid*.

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changes relating to the reporting requirements of the FSCA.[291] It further confirmed that reporting mechanisms would be developed as part of the supervisory framework, which development would be done in conjunction with consultation with the industry.[292]

In order to comply with the requirements in terms of the FSRA to monitor whether financial institutions are delivering fair outcomes for customers, the FSCA requires access to meaningful and reliable TCF indicators.[293] In line with this requirement, the FSCA relies on CBRs, which were introduced by the FSB in December 2016.[294] CBRs constitute a set of market conduct reports that form part of the statutory returns for long- and short-term insurers. By making use of a risk-based approach and to ensure that financial institutions have adequate time to address internal systems and data limitation challenges, financial institutions have had a two-year transitional period in which to achieve full compliance with reporting requirements.[295]

These returns are now to be completed and submitted to the FSCA on a quarterly basis.[296] The submission of these reports form part of the offsite supervision framework for insurers[297] and the CBR's comprise various sections of the lifespan of a policy from inception to claim. The templates were revised as recently as 2021, and insurers have been submitting returns as per the amended template as of 1 May 2021. Amendments in terms of CBR reporting is to be therefore ongoing.[298]

The change in the information gathering requests intensifies the importance of the supervision goal from the perspective of proactively identifying potential conduct risks within specific financial institutions or within the industry as a whole.[299] A large component of information gathering comes from customer complaints data. The FSCA sets the rules in terms of the mechanisms through which complaints are managed by financial institutions, albeit within the boundaries of the legislative provisions.[300] The FSCA also plays an oversight role from the

[291] FSB *TCF Baseline Study* 8.
[292] *Ibid*.
[293] FSB *CBR's Revised Categorisation* 1.
[294] *Ibid.*
[295] *Idem* at 2.
[296] *Idem* at 1.
[297] *Ibid.*
[298] *Idem* at 2.
[299] Treasury *Explanatory policy paper accompanying COFI* 93.
[300] *Idem* at 94.

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perspective of the ombud schemes when gathering information regarding complaints from financial consumers.[301]

From the financial institution's perspective, the insurance industry had to adjust to the requirements set out by the FSCA to adopt standards and align with the requirements for the future. Some of these changes were in relation to structure, skills, technology, culture, data and reporting.[302]

While there are aspects of TCF which require mere compliance, such as where the rules are specific, implementing TCF in a manner that aligns with it purpose, is not a compliance function or project.[303] Implementing TCF is also not a once-off initiative. It is expected that this will be an evolving concept which will form part of a financial institution's day to day business.[304] There is an expectation that financial institutions must be in a position to provide evidence supporting the fact that they are treating their customers fairly and that TCF has been embedded as part of their organizational culture.[305] This will be done by management information, in effect, reports which enable the monitoring and measurement of a financial institution's ability to deliver in terms of the TCF outcomes.[306] Qualitative and quantitative management information will be required. The requirement is not merely to have the management information available, but to demonstrate that same is being used effectively – meaning that there is an analysis of same with the intention of identifying and rectifying customer conduct risks.[307]

Financial institutions are now required to review their existing structures to ensure capability within the revised regulatory requirements. They must compile and analyse information in order to effect remedial action, where necessary.[308] These institutions are expected to up-skill their existing resources to ensure that staff are adequately trained and have the relevant skills and knowledge in complaints, relevant complaints subject matters, the principles of TCF, and in the regulatory provisions relating to compliance and reporting.[309]

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[301] *Ibid.*
[302] *Ibid.*
[303] FSB *TCF Road Map* 20.
[304] *Ibid.*
[305] FSB *CBR's Revised Categorisation,* 2.
[306] *Ibid.*
[307] FSB *TCF Road Map* 21.
[308] FSB *TCF complaints management* 6.
[309] *Idem* at 7.

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The compliance requirements relating to reporting and the complexity of the information required has led firms to consider utilizing technology-based solutions.[310] As the reporting requirements have become more stringent, firms have initiated the development of central points for the deposit of data to enable and facilitate more consistent and accurate reporting.[311] These developments, in turn, require consideration of the laws relating to personal information and privacy – a matter that is not dealt with in this dissertation but deserves to be considered for future research purposes.

2.5. Final remarks and conclusion

The intention of the shifts in the regulatory environment specific to complaints management is to support the delivery of fair outcomes to customers within the financial services sector.[312] It is to ensure that monitoring becomes an enabler to establish that the outcomes are being achieved and to ensure that, if a risk of poor outcomes exists, there are steps to detect and mitigate such risk. The approach differs from the historic approach wherein random supervisory visits were done to determine compliance with the regulations and where addressing poor outcomes was a slow process, if initiated.[313] The supervisory approach has evolved and will continue to do so from the viewpoint of assessing whether financial institutions are conducting themselves in a manner that delivers the desired customer outcomes as opposed to assessing on compliance and prescriptive rule-based requirements.[314]

This approach has been supported by the ongoing requests from the FSCA for data through information gathering processes.[315] The historic requests remain, however the ability to detect conduct risks are not necessarily possible through the analysis of the regular report submissions.[316] This was the initial challenge and hence the need for change.

Managing an organisation's risk and ensuring compliance with regulatory requirements has always fallen within the ambit of the compliance role. With the changes which have taken place over the past three to five years, the question to be asked is whether the insurance industry still maintains the view that adherence to the changed market conduct rules and principles remain

[310] Ernst & Young *Financial Sector Regulation Act, implementing twin peaks and the impact on the industry* 12.
[311] *Ibid*.
[312] Treasury *Explanatory policy paper accompanying COFI* 11.
[313] *Ibid.*
[314] *Ibid.*
[315] *Idem* at 93.
[316] *Ibid.*

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a compliance exercise. While the key areas are theoretical in that processes, frameworks, and governance structures ought to be in place, the practical application thereof requires a robust regulatory approach with stringent and intrusive oversight practices to ensure compliance.

There are three simplistic ways for an insurer, as a financial institution, to consider market conduct risk, its monitoring, and its effective management: determine who should be managing conduct risk within an insurer; determine how conduct risk can be managed effectively and determine what should be measured and monitored to ensure customers are receiving fair outcomes. This means that greater reliance will be placed upon a financial institution to initiate, change, and implement practices which are aligned to the market conduct principles. However, the Regulator will utilise the tools available to it from a regulatory and supervisory perspective to establish how it will monitor and manage the respective financial institutions. A financial institution will therefore be expected to ensure that its processes, frameworks, and structures align to the regulatory requirements and that there is ongoing monitoring, reviewing, and an analysis of its data to detect and deal with any market conduct risks that may arise.

The above raises a number of questions on the impact of the new regulatory and legislative structures on insurers as regulated entities. Does compliance become an expensive resource to the business? Will financial institutions be expected to expand on their compliance capability on an institution-wide level to ensure adherence to the regulatory requirements of market conduct? I am of the view that the responsibility extends to all aspects of the business in line with the cultural reformation envisaged by TCF. The compliance function remains unchanged; however, the business must now adapt to incorporate market conduct into its operational strategy to ensure that all levels of the business are aligned to the principles and expectations of market conduct. The costs thereof are yet to be determined.

This chapter provided a high-level overview of the regulatory and legislative structure relevant to complaints management in the insurance industry. The components that were addressed included the reform and the structural changes. The next chapter deals with specific aspects related to complaints management in the insurance industry. It provides an evaluation of the specific aspect of the policyholder protection rules as well as the guidance provided by regulators relating to expected outcomes on the complaints management framework. It provides insight into the Conduct of Financial Institutions (COFI) Bill and whether a substantial change is expected.

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Chapter 3: Complaints management in the insurance industry

3.1. Introduction

This chapter deals with an evaluation of the policyholder protection rules, specific to complaints management within the insurance industry. The discussion extends to both the short-term and long-term PPRs. The anticipated outcomes of the COFI Bill as well as guidelines relating to outcomes of the complaints management framework.

3.2. Background

A customer's first attempt at resolving a complaint ought to be with the financial institution itself.[1] TCF outcome six states that customers should not face unreasonable post sale barriers when submitting a complaint.[2] In order to demonstrate alignment with this TCF outcome, a financial institution ought to have an effective process to manage its complaints.[3] Financial institutions are expected to use customer complaints as an important source of information to measure their delivery in terms of customer outcomes and to improve and enhance processes within the organization.[4] The regulatory framework would therefore be expected to provide guidance to financial institutions to ensure that there is a standard and consistent process which should be met. This was identified as a shortcoming of the historic regulations.[5] A revised standard was set per the amended regulations.[6]

The regulations impose specific obligations on financial institutions to develop and implement complaints handling processes as part of their daily operations.[7] The rules stipulate that insurers are to include further levels of escalation into their complaints management process should a customer be dissatisfied with the outcome of a matter following engagement with the insurer.[8] There are several ombudsman schemes which are in place to ensure that such complaints are dealt with fairly and efficiently.[9]

[1] Treasury *Draft Market Conduct Paper* 55.
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] FSB *TCF complaints management* 6.
[6] *Policyholder Protection Rules* 2019 chapter 7.
[7] Millard (2011) "Bespoke justice? On financial ombudsmen, rules and principles" *De Jure* 236.
[8] *Policyholder Protection Rules* 2019 chapter 7, rule 17.6.5.
[9] FSCA *Regulatory Strategy* 57.

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Although the FSCA is the market conduct regulator, and complaints and the management thereof is of relevance to its mandate, the FSCA is not intended to handle complaints for financial customers when these are brought against financial institutions, unless the complaint also involves a contravention of a financial sector law.[10] The Regulator does, however, require insight into concerns or trends relating to customer conduct.[11] Its intention is not to deal with disputes relating to the outcome of a claim, such as repudiated claims or disputes relating to the settlement of a claim.[12] The expectation is to ensure that the insurance industry is adequately regulated to deal with these disputes in a fair and transparent manner.[13]

The FSCA is nevertheless not removed from these complaints. It works closely with the ombudsman schemes to monitor, track, and respond to the trends on specific types of complaints received.[14] The ombudsman schemes are also mandated to refer matters, where they have identified contraventions of the law, to the FSCA and so alert the Regulator when firms show a pattern of poor customer treatment, to enable the FSCA to act upon same.[15] Protecting a customer is therefore intended to be more than the FSCA merely responding to customer complaints. This still forms an important part of the FSCA building trust with the customer base of the market, and the aim is to deal with poor practices that customers are often oblivious to.[16]

As indicated in the previous chapter, the supervisory focus of the Regulator has shifted.[17] The FSCA intends on looking at the suitability of the product offering from the onset.[18] Dealing with a complaint and scrutinizing aspects – such as the sales process, correspondence between the financial institution and customer over the lifetime of the product, and claims processes – are usually interventions which happen too late.[19] These features still play a pivotal role in the FSCA understanding what the root cause of the problem is; however, the damage, from the perspective of poor customer outcomes, has already been done at this stage. By reviewing the

[10] *Ibid*.
[11] *Ibid*.
[12] *Ibid*.
[13] *Policyholder Protection Rules* 2019 chapter 7, rule 17.6.
[14] Treasury *A known and trusted ombud system for all* 16.
[15] *Ibid*.
[16] FSCA *Regulatory Strategy* 57.
[17] *Ibid*.
[18] *Ibid*.
[19] Section 70(2) of the FSRA.

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suitability of the product upfront, the FSCA will understand issues related to the governance structures and customer centricity within the financial institutions earlier rather than later.[20]

Complaints management was part of the reviews referred to in chapter two. Insofar as the insurance industry was concerned, the regulatory framework and the PPRs were parts of the legislative regime which needed to be reviewed.[21] The Regulator embarked on a special review (April to June 2014) to establish how the industry handled complaints and to understand how customers were treated.[22] The initial focus was the personal lines business, in effect individual customers and small and medium-sized enterprises.[23] The Regulator, through its review and engagements, adopted the TCF framework to ensure fair outcomes to customers within the financial services sector. The intention was to ensure that the industry is adequately regulated at all stages of the relationship between the customer and the financial services institution.[24]

Based on the review referred to earlier and regulatory changes implemented as discussed hereafter, the Regulator sought to standardize all complaints management to ensure consistency in the application of principles.[25] The purpose of the new regulations was specifically to improve market conduct within the industry and ensure the fair treatment of customers. One of these changes was the new PPRs, which were finally gazette into law on 15 December 2017. The rules were intended to have a phased implementation process.[26] The new rules make sweeping changes to the prior ones and affected personal lines policies as well as small commercial policies. The definition of a policyholder was also amended to include a potential policyholder.[27] These regulations formally incorporated the six TCF outcomes into law. As an example of importance and relevance to complaints management, the complaints management process evolved to include clear definitions and standards in terms of how complaints should be captured, reported, analysed, and attended to.[28]

[20] Treasury *Draft Market Conduct Paper* 30.
[21] Treasury *Twin Peaks in SA: Response & Explanatory Document* 10.
[22] FSB *TCF complaints management* 2.
[23] FSB *TCF Road Map* 7.
[24] *Policyholder Protection Rules* 2019 chapter 8.
[25] FSB *TCF complaints management* 1.
[26] FSCA *Proposed Amendments to PPR Consultation Report* 2.
[27] Treasury *Tranche 2 amendments to the short-term PPRs* 6.
[28] *Policyholder Protection Rules* 2019, rule 18.

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The Regulator subsequently prescribed guidelines for the definition of a complaint and the components of a complaints management framework.[29] These are set out and discussed below: A consistent regulatory definition of "complaint"; standards and requirements for firms to implement internal complaints management processes; the requirements for TCF-aligned categorization of complaints; the requirements for engagement between firms and ombudsman schemes; the requirements for reporting complaints information to the Regulator; and the requirements for public reporting of complaints information.

3.3. An overview of the elements of complaints management

The concept that recourse should be available to a customer who is dissatisfied has been entrenched within the industry, meaning that a customer who is of the view that he or she is being treated unfairly by a financial institution has the right to complain about the behaviour of the financial institution.[30] The firm has an opportunity to respond to the customer's complaint.[31] Generally, an independent body, such as an ombudsman, may resolve the dispute if a customer is still dissatisfied after engagement with the financial institution. There is also a right of appeal or review.

Recourse starts with a complaint. An important question arising out of the above summary of the process is whether there is consistency within the financial services industry regarding what constitutes a complaint and when same ought to be recorded and reported. This was an area identified and highlighted in the complaints review undertaken by the FSB in 2012. A proposal in relation to specific definitions was put forth to the financial services industry, which proposal was later accepted and entrenched into the regulations. A complaint is defined as

> "an expression of dissatisfaction by a complainant, relating to a product or service provided or offered by a financial institution, or to an agreement with the financial institution in respect of its products or services and indicating that –
>
> (a) the financial institution or its service provider has contravened or failed to comply with an agreement, a law, a rule, or a code of conduct which is binding on the financial institution or to which it subscribes;

[29] FSB *TCF complaints management* 14.
[30] Feasibility *A report prepared for the FSB, TCF complaints management* 30.
[31] *Policyholder Protection Rules* 2019 chapter 8, rule 18.3.1(f).

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(b) the financial institution or its service provider's maladministration or wilful or negligent action or failure to act, has caused the complainant harm, prejudice, distress or substantial inconvenience; or

(c) the financial institution or its service provider has treated the complainant unfairly and regardless of whether such an expression of dissatisfaction is submitted together with or in relation to a customer query."[32]

A complainant is

> "a person who has submitted a specific complaint to a financial institution or, to the knowledge of the financial institution, to the financial institution's service provider and who –
>
> (a) is a customer or prospective customer of the financial institution concerned and has a direct interest in the agreement, product or service to which the complaint relates; or
>
> (b) has submitted the complaint on behalf of a person mentioned in (a), provided that a prospective customer will only be regarded as a complainant to the extent that the complaint relates to the prospective customer's dissatisfaction in relation to the application, approach, solicitation or advertising or marketing material contemplated in the definition of 'prospective customer'."[33]

Other important definitions include the following:

> "'Customer query' means a request to the financial institution by or on behalf of a customer or prospective customer, for information regarding the financial institution's products, services or related processes, or to carry out a transaction or action in relation to any such product or service."[34]

> "'Goodwill payment' means a payment by a financial institution to a complainant as an expression of goodwill aimed at resolving a complaint, but where the financial institution does not accept liability for any financial loss to the customer as a result of the matter complained about."[35]

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[32] FSB *TCF complaints management* 3.
[33] *Ibid.*
[34] *Ibid.*
[35] *Ibid.*

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"'Compensation payment' means a payment, other than a goodwill payment, by a financial institution to a complainant to compensate the complainant for a proven or estimated financial loss incurred as a result of the financial institution's contravention, non-compliance, action, failure to act, or unfair treatment forming the basis of the complaint, where the financial institution accepts liability for having caused the loss concerned."[36]

"'Compensation payment' excludes –

(a) payment of amounts contractually due to the complainant in terms of the financial product or service concerned, or

(b) refunds of amounts paid by or on behalf of the complainant to the financial institution where such payments were not contractually due but includes interest on late payment of amounts or refunds referred to in (a) or (b)."[37]

The definitions set out above do not align to existing legislation such as the FAIS Act. The FAIS Act provides the following definition of a complaint:

"In terms of the FAIS Act, a 'complaint' means a specific complaint relating to a financial service rendered by the FSP or a representative of the FSP, to the complainant on or after the date of commencement of the FAIS Act, and in which complaint it is alleged that the FSP or representative … has contravened or failed to comply with a provision of the FAIS Act and that as a result thereof the complainant has suffered or is likely to suffer financial prejudice or damage; or has willfully or negligently rendered a financial service to the complainant which has caused prejudice or damage to the complainant or which is likely to result in such prejudice or damage; or has treated the complainant unfairly".[38]

The definitions also do not conform to the definitions set out in some of the ombudsman schemes.[39] The intention, however, is for the definitions to align as the landscape evolves. Some of the existing legislation had imposed requirements on financial institutions to have a complaint handling process in place, which processes would set specific requirements relating to standards for handling complaints – for example, the General Code of Conduct under the

[36] *Ibid*.
[37] *Idem* at 20.
[38] Act 37 of 2002.
[39] FSB *TCF complaints management* 20.

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FAIS Act set out the requirements.[40] The high level expectation in terms of complaint handling are that a financial institution ought to have a complaints process in place, which process should to be readily available to customers.[41] The complaints ought to be dealt with in a fair, transparent and timely manner.[42] A financial institution is at liberty to deal with a complaint within its structures.[43] Should a complainant be dissatisfied with the outcome, the complainant has a right of recourse to an external body.[44] The financial institution should notify the complainant of these external bodies and provide the relevant timelines for lodging such complaint.[45]

Once these themes have been fully described and implemented, a review of all applicable laws will be done in order to identify gaps and to ensure that all legislation, subordinate legislation and codes are aligned.[46]

Based on these guidelines set out for customer protection as well as the changes within the financial sector in South Africa, it is clear that the changes are intended to move to a more vigorous and efficient process, specific to addressing market conduct issues or concerns.[47] Whilst it is noted that many customer complaints are dealt with by insurers through their own complaints management processes, it is important that the Regulator have sight of these in order to ensure the consistent and effective handling of fair outcomes by all financial institutions.[48]

Complaints management and its reporting mechanism can identify broader concerns and trends which require the mitigation of action or remediation thereof.[49] Complaints management and any root cause analysis and remedial action contribute to the overall effectiveness of a conduct of business framework.[50] Complaints are considered part of the daily functioning of a financial institution. Tracking and reporting on same will enable a financial institution to identify a concern, for example complaints that take a lengthy time to resolve could be an indication of

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[40] *Idem* at 18.
[41] SAIA *Code of Conduct* 19.
[42] *Ibid*.
[43] *Ibid*.
[44] *Ibid*.
[45] *Ibid*.
[46] FSB *TCF Road Map* 16.
[47] FSB TCF *complaints management* 3.
[48] *Ibid*.
[49] FSB *CBR's Revised Categorisation* 2.
[50] FSB *TCF complaints management* 16.

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ineffectiveness.[51] On the other hand, a framework or process in which there are no complaints could be as a result of an undesirable process or one that fails to identify conduct risks.[52] It is therefore important that there be a clear mandate and process, which is what the Regulator sought to achieve in Chapter 8 of the PPRs.[53] This is an important indication that the complaints process of framework must be clearly documented and customers must be made aware of what their avenues are when they are dissatisfied.[54]

As indicated on numerous occasions, the TCF outcomes are a set of principles against which financial institutions will be measured to establish how they conduct their business in relation to their customers.[55] The intention is to utilise complaints data to measure the progress of a financial institution to deliver on the TCF outcomes.[56] In this regard, complaints are to be categorised in accordance with the TCF categories.[57]

The expectation is that financial institutions categorize their complaints in accordance with the six TCF outcomes.[58] This would be a measure for the financial institution as well as the FSCA in relation to the manner in which a financial institution performs against market conduct outcomes. It would further support the regulatory and supervisory approach in determining its effectiveness.[59] It is anticipated that future reporting from a regulatory and public domain perspective will require the categorization of complaints in terms of TCF outcomes.[60] For purposes of compliance with the regulation, it is important that complaints be categorized as such.[61] However, should financial institutions see value in further granular categorization, the FSCA would welcome same.[62] This would illustrate that financial institutions are committed to the strategy and will be more effective in delivering on fair outcomes to customers.[63] It would also support the culture aspect of a financial institution confirming that the institution does incorporate the voice of the customer into their daily operations.[64]

[51] *Ibid.*
[52] *Ibid.*
[53] Treasury *Explanatory policy paper accompanying COFI* 50.
[54] FSB *TCF complaints management* 3.
[55] *Idem* at 11.
[56] *Ibid.*
[57] *Ibid.*
[58] FSB *TCF complaints management* 9.
[59] *Ibid.*
[60] *Ibid.*
[61] *Ibid.*
[62] *Ibid.*
[63] *Ibid.*
[64] *Ibid.*

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The specific outcomes of most relevance to the substantive contents of complaints and the complaints management process itself, are outcomes 1, 2, 3, 4, 5(a) and 5(b). The first outcome specifically relates to the culture of financial institutions. In the context of complaints management, this means that the culture of firms is evaluated to establish whether the customer is considered and the impact of outcomes to customers as part of the business strategy.[65] TCF has been part of the framework for some time now. This specific outcome is expected to be reported upon, should complaints be received and categorised as such. A typical example of a complaint relating to this outcome would be where a customer states that the financial institution has no regard for the feedback which was provided. The financial institution has made a decision in terms of an outcome and will not have any further regard for input from the customer, despite the customer having confirmed that not all information was considered in evaluating the outcome of the claim.

The second outcome deals with complaints relating to the design of a product or service and this category is intended to include complaints which indicate that specific aspects of a product are unfair, complex, or have the inability to perform per the target market for which they were intended.[66] The third outcome includes complaints on the information which is provided to a customer. The complaints could be in relation to the content of the information, the manner or medium in which it is provided.[67] The information could potentially be unclear, confusing, too complex for the target market to understand, misleading, or incomplete.[68] This would also extend to include a failure to provide the information or a failure to provide same when required to do so.[69] TCF has been part of the framework for some time now. Insurers do report on this outcome and same forms part of complaints reporting via conduct of business returns. This is a mechanism for providing quarterly reports to the regulator.

Outcome four is intended to relate to complaints where the advice which was provided to a customer did not take into consideration the actual needs of the customer.[70] The specific complaint would extend to include instances where the advice was misleading or factually incorrect and was not provided in accordance with the customer expectations from a timeline perspective.[71] These types of complaints could illustrate that the adviser was unskilled, had a

[65] *Ibid*.
[66] *Ibid*.
[67] *Ibid*.
[68] *Idem* at 12.
[69] *Ibid*.
[70] *Ibid*.
[71] *Ibid*.

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conflict of interest, or lacked the appropriate knowledge to assist the customer.[72] A financial institution's model and the manner in which it sells and markets products, specific to its financial advisors or agents could create poor customer outcomes.[73] This could arise when a financial advisor is incentivised by a financial institution in terms of, for example, the number of policies sold in any given period.[74] The financial adviser is therefore conflicted in that the focus would be on making a high number of sales as opposed to having a focus on the quality of the sale. The quality of the sale would ensure that there is compliance with the requirements relating to advice and disclosures to the customer to ensure that the customer receives clear, transparent and correct information to make a decision. The reporting relating to these types of complaints should extend to include the relevant distribution channels to establish whether the manner in which the product was sold or is being sold is suitable to the target market.[75] TCF has been part of the framework for some time now. Insurers are expected to report on this outcome. As noted above same forms part of complaints reporting via conduct of business returns. This is a mechanism for providing quarterly reports to the regulator.

TCF Outcome 5(a) relates to complaints regarding product performance. This category of complaints demonstrates that the financial institution's intention and the customer expectation relating to the manner in which a product performs are not aligned.[76] These types of complaints would generally be in relation to investments or savings products.[77] TCF Outcome 5(b) deals with complaints relating to customer service. This category of complaints relates to the financial institution's ability to deal with the administrative requests of a customer.[78] These extend to include the manner in which a financial institution's staff have treated the customer, in effect timeous responses to requests, professional etiquette, etc.[79] A financial institution's service providers' service toward a customer would also be included in this category.[80] As noted above same forms part of complaints reporting via conduct of business returns. This is a mechanism for providing quarterly reports to the regulator.

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[72] *Ibid*.
[73] Treasury *Explanatory policy paper accompanying COFI* 49.
[74] FSB *TCF complaints management* 12.
[75] *Ibid*.
[76] *Ibid*.
[77] *Idem* at 13.
[78] *Ibid*.
[79] *Ibid*.
[80] *Ibid*.

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3.4. An overview of the challenges relating to complaints management

3.4.1. The need for clear guidance as opposed to high-level policies

The external bodies that dealt with complaints had a detailed standardized process, whereas insurers were provided high level processes which were not clear.[81] Customers were not familiar with the internal processes for insurers.[82] The Regulator therefore sought to standardize the complaints management framework with clear guidelines and mandatory structures to ensure consistency and standardization amongst all players within the industry.[83] The writer is of the view that this is concerning. The COFI Bill is intended to establish and consolidate specific requirements which financial institutions have to meet. The implementation of the TCF principles within the Bill will enforce the principles and make same binding across all financial institutions. The intention is to provide customers with the assurance that they are dealing with financial institutions where TCF is central to the corporate culture. The historic issue which existed was that the rules were applicable, however, the enforcement of same was not monitored or tracked. Therefore, is this not another set of rules to be enforced without a manner to establish implementation.

With the COFI Bill, the National Treasury is hoping to ensure that South Africa's financial sector continues to provide consumers and businesses with fair services and good value products that enable them to receive and make payments, and to save, borrow and insure themselves against daily risks.

Under the proposed legislation, financial products and services marketed and sold in the retail market will have to be designed to meet the needs of identified customer groups and targeted accordingly. These principles are already entrenched in current legislation like the Policyholder Protection Rules in the Insurance industry. COFI will standardise the principles to apply to all customers in the financial sector. All customers will be provided with clear information and kept appropriately informed before, during and after the point of sale; and when advice is given, it will have to be suitable to the customer's circumstances. Customers will also not face unreasonable post-sale barriers when they want to change products or switch providers.

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[81] *Idem* at 14.
[82] *Ibid*.
[83] *Ibid*.

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3.4.2. The need for a consistent regulatory definition of "complaint" and a comprehensive definition of "reportable complaint"

An important component to ensure that a complaints management framework is effective is a uniform definition of a complaint, and in this regard a definition that was standard to all stakeholders within the insurance sector was needed.[84] Complaints were not defined consistently within the financial services industry and it was established that the manner in which various stakeholders within the financial services industry handled complaints was inconsistent.[85] The result was the formulation of the definition of a complaint and the adoption of same into the PPRs which define a "complaint" as

> "an expression of dissatisfaction by a complainant, relating to a product or service provided or offered by a financial institution, or to an agreement with the financial institution in respect of its products or services and indicating that –
> (a) the financial institution or its service provider has contravened or failed to comply with an agreement, a law, a rule, or a code of conduct which is binding on the financial institution or to which it subscribes.
> (b) the financial institution or its service provider's maladministration or willful or negligent action or failure to act, has caused the complainant harm, prejudice, distress or substantial inconvenience; or
> (c) the financial institution or its service provider has treated the complainant unfairly and regardless of whether such an expression of dissatisfaction is submitted together with or in relation to a customer query."[86]

The complaints review illustrated that the definition of a "complaint" within the insurance industry was not clear or aligned.[87] Several sets of feedback revealed that some insurers dealt with queries as complaints, whilst some dealt with complaints as queries.[88] It was therefore essential that the definitions of a query and a complaint be designed to ensure consistency of its interpretation and therefore its application. The above sets out the first step in attaining consistency in the legislation. The intention is to provide clarity and certainty regarding what should be considered a complaint. In order for an instance to be considered a complaint, all

[84] *Idem* at 8.
[85] *Idem* at 14.
[86] *Idem* at 8.
[87] *Idem* at 3.
[88] *Ibid*.

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requirements would need to be met.[89] In my view, the definitions have expanded the scope for complaints which is good practice from a market conduct point of view. It forces financial institutions to consider all matters that fall within the ambit of the definition and establish whether same can be dealt with as a complaint or query or both, and where it is considered both it should not be excluded from the definition of a complaint.[90]

Whilst it is acknowledged that the definition of a complaint is now clearer, there is a perceived shortcoming with regard to how complaints are reported. My view on this statement is simply related to the definition of a "reportable complaint" which

> "means any complaint other than a complaint that has been –
> (a) upheld immediately by the person who initially received the complaint;
> (b) upheld within the financial institution's ordinary processes for handling customer queries in relation to the type of agreement, product or service complained about, provided that such process does not take more than five business days to complete from the date the complaint is received; or
> (c) submitted to or brought to the attention of the financial institution in such a manner that the financial institution does not have a reasonable opportunity to record such details of the complaint as may be prescribed in relation to reportable complaints."[91]

This definition created a shortcoming as financial institutions do not have to report complaints, although valid, which were resolved within five business days. This likely creates inefficiencies in complaints handling – purely on the basis of handling a complaint within the shortest time possible to prevent reporting of same. Surely it could not be driving the correct behaviour from a market conduct perspective. In addition, it is difficult to determine the need for this differentiation, considering the outcome and intention of market conduct regulation under the new dispensation. The capturing and reporting of complaints are an important aspect of the process in that same allow the Regulator as well as financial institutions the opportunity to analyse, monitor and effect root-cause analyses with the aim of instituting remedial action, where necessary. Not having included all complaints in the definition of a reportable complaint is disappointing.

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[89] *Ibid*.
[90] *Ibid*.
[91] FSB *TCF complaints management* 5.

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3.4.3. Standards and requirements for firms to implement internal complaints management processes

The review of market conduct practices and complaints handling clearly illustrated that there was a need to standardize the regulation of same to ensure consistency in handling, reporting, monitoring and remediation.[92] The process could take several months to resolve, and the understanding is that there should be a time element attached to such a process.[93] In order to ensure that there is compliance by a financial institution with TCF outcome six, it was necessary for the development, implementation and effective monitoring of internal processes relating to complaints handling.[94]

TCF outcome six, specific to complaints, states that customers should not face unreasonable post sale barriers when trying to lodge a complaint.[95] An important aspect was the development of a complaints management process (CMP) which sets out how a financial institution would deal with its complaints in a fair and transparent manner.[96] A financial institution ought to decide how to structure its CMP based on its customer model and the complexity of its business. The requirements and standards that it is required to meet are important: the CMP must be a Board approved process; it must be accessible to all staff as well as external parties who deal with customers; all individuals who interact with the financial institution's customers must be trained on the CMP; the financial institution must allocate a senior resource to have oversight of the CMP, its implementation and monitoring; handling of complaints in terms of the CMP must be allocated to staff who are adequately trained and skilled to do so.[97] The responsible individuals must have knowledge of, and be experienced in, TCF approved behaviour towards customers and the relevant legal and regulatory aspects.[98] The CMP must have a process for the acknowledgement of a complaint, timelines as well as the process setting out how the complaint will be evaluated and a decision reached.[99] Same must include further channels of escalation or recourse available to the complainant, should the complainant be dissatisfied with the outcome of the financial institution's decision.[100] The process must include

[92] *Ibid*.
[93] *Idem* at 6.
[94] *Idem* at 5.
[95] *Idem* at 1.
[96] *Idem* at 6.
[97] *Idem* at 7.
[98] *Ibid*.
[99] *Ibid*.
[100] *Ibid*.

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the details of the individual handling the complaint at the financial institution, should there be a need for contact by the complainant.[101] There must be adequate communication in terms of progress and feedback in terms of timelines in order to manage expectations.[102] Should a complaint take longer that the timeline stipulated in the CMP, the complainant must be provided with feedback of the delay, reasons for delay and revised timelines relating to the outcome.[103] Upon a complaint not being in favour of the complainant, or providing an outcome favourable to the complainant, the financial institution must provide detailed reasons for the decision which was reached, in addition to the further channels for escalation.[104] If feasible, an internal dispute forum should be formulated to accommodate internal discussions on complicated or complex complaints.[105] This forum, from a decision-making perspective, should be impartial to the initial handling of the complaint.[106]

The outcome which was sought to be addressed via the TCF outcome was the unreasonable procedural barriers that a firm imposed to make the complaints process extremely difficult for a customer.[107] Such examples include short timelines, lengthy notice periods, inefficient communication mechanisms, and administrative delays.[108]

Chapter 8 of COFI has a specific focus on post sale barriers and the impact on the customer specific to complaints management.[109] The Chapter requires a consistent approach by financial institutions once a customer has purchased a product or entered into a contract with a financial institution.[110] It sets out the principle that a financial institution must not impose unreasonable barriers should a customer wish to switch or exit.[111] This is set out in the following extract of the Bill:

> *"**71.** (1) Financial institutions may not impose unreasonable post-sale barriers on financial customers that may prevent customers from holding a financial institution accountable for its contractual obligations, expectations created that are not being met,*

[101] *Ibid.*
[102] *Ibid.*
[103] *Ibid.*
[104] *Idem* at 8.
[105] *Ibid.*
[106] *Ibid.*
[107] Feasibility *A report prepared for the FSB, TCF Discussion Paper* 30.
[108] *Ibid.*
[109] Treasury, Explanatory policy paper accompanying COFI *Bill* 21.
[110] Treasury, Explanatory policy paper accompanying COFI *Bill* 21.
[111] Treasury, Explanatory policy paper accompanying COFI *Bill* 21.

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or perceived unfair treatment pertaining to a financial product or financial service that is being provided."

There are clear guidelines for claims handling processes where applicable.[112] Further entrenched in the chapter are the requirements for complaints handling processes within a financial institution as well as its interactions with the relevant ombudsman schemes as well as the requirements for the gathering of information through complaints which are utilized.[113] This is set out in the following extract of the Bill:

"74. A financial institution must—

a. provide acceptable levels of service support for the financial products and financial services provided, including in relation to responses to enquiries and any transaction or engagement that occurs after the initial sale of a financial product or financial instrument or the initial provision of a financial service to a financial customer;
b. provide service that is fair, reliable, and transparent and consistent with the reasonable expectations of the financial customer that have been created by the information and representations provided by or on behalf of the financial institution to the financial customer; and
c. provide acceptable levels of protection of safety and security in relation to the financial products and financial services provided and in relation to a customer's personal information."

The standards are expected to be made available, upon request from the Regulator.

3.4.4. Requirements for TCF-aligned categorization of complaints

Since the period of time that has passed since the implementation of the categorization of complaints, it has become entrenched in day-to-day operations in that there is an expectation when reporting to the regulator on a quarterly basis that this form part of the submission. A failure to do so renders an insurer non-compliant. At this stage, the reporting is limited to insurers who write business within the personal lines class of business. The intention, however, is to extend the scope to include all classes of business.

[112] Treasury, Explanatory policy paper accompanying COFI *Bill* 21.
[113] Treasury, Explanatory policy paper accompanying COFI *Bill* 53.

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3.4.5. Requirements in relation to the engagement between firms and ombudsman schemes

Although the complaints management framework specific to the ombudsman schemes are dealt with in detail in chapter four, a brief overview in order to deal consistently with the aspects identified by the Regulator alluded to earlier.[114]

The final outcome of the evolution of the ombud schemes and the structure is still awaited. However, the manner in which financial institutions engage with the ombud schemes is already provided for in some of the existing regulations.[115] Financial institutions are to ensure that the details of the relevant ombudsman are clearly and transparently communicated to customers.[116] This must occur at all stages of the product life cycle. Ideally, financial institutions should be able to deal with a complaint and resolve it without the need for the ombudsman making a final determination or ruling.[117] However, a complainant may elect to approach an ombudsman as opposed to the financial institution first, because the complainant is at liberty to do so without unduly delaying the process.[118]

It is expected that financial institutions must engage in open and honest communication with the ombudsman in order to resolve complaints.[119] Financial institutions should have records and demonstrate that they analyse complaints dealt with through the ombudsman schemes.[120] This is an important aspect of complaints handling, specific to financial institutions understanding and establishing reasons for an ombudsman making a decision contrary to their own.[121] It is important to establish whether there is a process failure or risks within their own products and services.[122] Should this be the case, remedial action will be required in order to prevent poor customer outcomes in the future.[123]

3.4.6. Requirements for reporting complaints information to the Regulator and public

As discussed earlier, complaints reporting is a vital aspect of market conduct in that an effective system with adequate monitoring serves as an early warning mechanism to the Regulator,

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[114] See par 3.2 above.
[115] FSB *TCF complaints management* 15.
[116] *Ibid*.
[117] *Ibid*.
[118] *Ibid*.
[119] *Ibid*.
[120] *Ibid*.
[121] *Ibid*.
[122] *Ibid*.
[123] *Ibid*.

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which is now the FSCA.[124] Receiving and analysing complaints data is intended to provide insight into market conduct risk, trends relating to customer risk, regulatory gaps and to establish whether its measures are effective.[125] The FSCA must utilize the information to the extent that it is expected of financial institutions to utilize same, in effect for purposes of effecting remedial action, improving or enhancing TCF outcomes for customers, and to prevent poor outcomes from recurring.[126]

The FSCA should utilize the information for purposes of remedial action at the level of the financial institution, or to establish whether it is an industry wide issue and ensure remedial action at an industry level.[127] The complaints information supports the FSCA in understanding the extent to which supervision should take place and which particular profile of financial institutions should be an area of priority.[128] In essence, complaints reporting is the tool which supports the FSCA in its facilitation of principles relating to risk-based, proportional, proactive and pre-emptive supervision.[129]

Complaints data should be categorized in accordance with the TCF outcomes and in respect of data relating to volume; timelines relating to outstanding complaints; the status of complaints; complaints finalized, upheld, or rejected; and the manner of resolution; to name but a few examples.[130] Financial institutions should also track volumes over periods to establish whether the data indicate certain trends, and to determine whether there is an increase or decrease in complaints.[131] The data may further be analysed to determine the reasons for the trend, for example, whether same can be attributable to an event, a process or requirement.[132] A financial institution will be expected to provide information and detail to the FSCA relating to these trends, upon request.[133] A financial institution must be in a position to justify its findings and provide feedback on how a negative trend will be mediated.[134]

Although the above may seem like good business practices, internal monitoring has now seemingly become a regulatory obligation where the FSB's requirements on TCF complaints

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[124] *Idem* at 16.
[125] *Ibid*.
[126] *Ibid*.
[127] *Ibid*.
[128] *Ibid*.
[129] *Ibid*.
[130] *Idem* at 17.
[131] *Ibid*.
[132] *Ibid*.
[133] *Ibid*.
[134] *Ibid*.

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management are extrapolated to the new regulatory dispensation. As indicated, the FSCA may then require the financial institution to report on its internal monitoring and findings and it would be possible that an institutions internal processes (and quality of monitoring outcomes) are found wanting. On the one hand, alignment with market conduct requirements is the prerogative of the institutions, overseen by the Regulator. On the other hand, as indicated in chapter two, the FSRA provide for intrusive regulatory practices, and it would be valuable to see whether the FSCA will communicate it expectations in respect of internal monitoring and reporting of same.

Financial institutions may, in future, be required to publicly disclose the elements of their own complaints data.[135] As stated above, it is anticipated that the publication of complaints data will serve as motivation for financial institutions to enhance the delivery of their products and services to better suit customers.[136] Positive feedback relating to complaints data serves as positive marketing for a financial institution.[137] The reasoning is that the publication of data will act as a deterrent to poor customer outcomes.[138] The expectation is that financial institutions will compete over the quality of customer experience which they deliver.[139]

However, there is still extensive work which is to take place prior to reaching this stage of the strategy. It remains to be seen how the industry will react to the mandatory disclosure of complaints-related information to be public and, if forced to do so, how this will impact internal practices. This matter is dealt with in more detail below.[140] This is over and above legal (and even constitutional) challenges that may potentially be raised. This dissertation does not deal with the last question but recommend that the situation be monitored, and future research conducted on this topic. This aspect did not form part of the industry reviews. However, the writer is of the view that there will be engagement with the industry when the regulator is ready to table this discussion.

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[135] *Ibid*.
[136] *Ibid*.
[137] *Ibid.*
[138] FSB *TCF Road Map* 24.
[139] *Ibid.*
[140] See par 3.5.2 below.

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3.5. Examples of specific changes related to the PPRs based on TCF principles

3.5.1. Performance of a product and the needs of the customer

The principles of TCF are now entrenched in the PPRs.[141] This implies that there is a statutory duty to ensure that the insurance industry upholds a certain standard of fairness when dealing with their customers. As per Rule 1.4(e), it has now become the responsibility of the insurer to ensure that, if a customer is provided with a product, the product performs as the customer had expected it to perform at the inception of the policy. The consequences of non-compliance are broad as it provides a customer with a defense in terms of estoppel, which is in essence to hold an individual or entity accountable for a misrepresentation.[142] This is the applicable position, despite the customer having agreed to a policy which sets out terms and conditions as well as the nature and obligations of all parties.[143]

This would imply that, if a customer complains after a claim has been lodged and the outcome is that the product does not meet the client's need, the insurer's decision to repudiate a claim could be overturned.[144] The analysis of the complaint would have to illustrate that the customer was led to believe that there was cover even though, in actual fact, the policy document with which they were issued excluded such cover. The PPRs would hold the insurer liable as a market assessment ought to have been done to establish whether the product being sold adequately meets the needs of that specific market segment.[145] It is the insurer's responsibility to ensure that the customer understands the entire agreement.[146]

If an insurer chooses to outsource this responsibility to a broker, it still remains the insurer's responsibility to ensure that the appointed broker knows and understands its role and responsibility relating to advice from a customer perspective.[147] The immediate reaction to this from an industry perspective is that this places an unfair burden on an insurer and dilutes the role of the broker or intermediary.[148] In my view, this argument does not absolve the broker from all responsibility. The FAIS Act provides an overview of the requirements relating to advice to ensure that a customer is in a position to make an informed decision based on the

[141] FSB *Overview of proposed amendments to the regulations and PPR*.
[142] *Ibid*.
[143] *Ibid*.
[144] FSB *Tranche 2 amendments to PPR* 2.
[145] FSB *TCF complaints management* 12.
[146] *Ibid*.
[147] *Ibid*.
[148] *Ibid*.

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advice provided,[149] as it regulates the manner in which financial service providers render advice to financial customers.[150] Any person therefore who renders financial service must do so in accordance with the conduct of business requirements that are applicable within the financial services industry.[151]

The legislation aims to create greater communication and collaboration between a broker and its insurer.[152] There is certainly a greater onus placed on the insurer, however, if an insurer elects to have an intermediated model, insurers and intermediaries must strategise to determine what would best suit an end customer.[153] Ensuring that a customer receives clear, concise and transparent information when a policy is being incepted limits the risk for underwriting at claims stage.[154]

The FAIS Act as well as TCF outcome 2 provide that a financial institution must take all reasonable measures to ensure that information is obtained from the customer in order to understand what the need is.[155] It is upon this basis that a financial institution would be adequately equipped to provide a customer with a product that is suitable to a customer need. The information would be required in order for the financial institution to conduct an analysis to establish what the need of the customer is and provide advice or a product that suits that need. The contention arises when a claim is received, and a customer has a reasonable expectation that there will be cover based on the advice that they were given at the inception and/or sale of the insurance policy. In most instances, the claim would be repudiated based on a policy limitation or exclusion. The decision on the claim is reliant upon the circumstances of the incident in relation to the scope of cover afforded in terms of the policy. However, when a complaint is lodged, a customer would generally raise the issue of the expectation created at inception versus the performance of the product when a claim occurs. The complaints process would place reliance on a financial institution or an ombudsman scheme evaluating the value chain to establish whether the product was suitable to the need of the customer. If it was established that there was a failure at inception, same allows for an equity decision to be considered as the financial institution's failure at inception resulted in an unfair outcome to the customer. The General Code of Conduct makes it clear that the information provided must be

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[149] Mochesane (2014) "The legal protection of clients against insurance advisors" 3.
[150] Section 7(1) of the FAIS Act.
[151] Reinecke, Van Niekerk and Nienaber (2013) *SA Insurance Law* 512.
[152] FSB *TCF complaints management* 12.
[153] *Ibid*.
[154] *Ibid*.
[155] Section 9 of the FAIS Act.

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adequate and appropriate in the circumstances and take into account the factually established or reasonably assumed level of knowledge of the client.[156] This outcome is also entrenched in the FAIS Act.[157]

The PPRs currently apply only to natural persons or companies who have an annual turnover of R 2.5 million or less, and there is no doubt that the legislator will eventually expect that all financial institutions treat all customers in the same manner.[158] There is therefore an onus on insurers and brokers or intermediaries to collaborate in order to ensure that the customer's needs are met throughout the insurance value chain.[159]

3.5.2. Aspects of non-disclosure and misrepresentation, and the consequences thereof

An insurer must provide details relating to the product or service offering in order for a customer to understand what product or service is being sold.[160] There are many different products with varying features which are offered by the financial services industry. Based on the complexity of the offerings, an insurer must disclose comprehensive information relating to the product or service to the customer.[161] A failure to do so would likely constitute a failure to disclose on the part of the insurer.[162] Should there be a failure to disclose and a claim is submitted, a reasonable expectation had been created and a failure to disclose would likely result in the mandatory payment of a claim.[163] Repudiation of the claim would be an unfair outcome to the customer due to the failure on the part of the insurer to provide comprehensive information upfront.[164]

The Long-Term and Short-Term Insurance Acts have provisions relating to non-disclosure.[165] In summary, these provisions state that an insurer may not repudiate on the basis of non-disclosure unless it can show that its assessment of the risk at sales or underwriting stage was materially affected.[166] The historic sections in the Long- and Short-Term Insurance Acts were identical in its wording:

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[156] Millard and Maholo (2016) "*Treating Customers Fairly: A new Name for Existing Principles*" *THRHR* 604.
[157] Section 9 of the FAIS Act.
[158] FSCA *Consultation report and comment matrix – PPRs* 34.
[159] Treasury "*Commencement date for the Insurance Act No. 18 of 2017*" 26 June 2018.
[160] FSCA *Consultation report and comment matrix – PPRs* 25.
[161] *Ibid.*
[162] *Ibid.*
[163] *Ibid.*
[164] *Ibid.*
[165] Section 59(1)(a) and section 53(1)(a) respectively.
[166] O'Connor and Ahmed "The Duty to disclose material information remains" 6 March 2019.

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"(a) Notwithstanding anything to the contrary contained in a short-term policy, whether entered into before or after the commencement of this Act, but subject to subsection (2) —

(i) the policy shall not be invalidated;

(ii) the obligation of the short-term insurer thereunder shall not be excluded or limited; and

(iii) the obligations of the policyholder shall not be increased, on account of any representation made to the insurer which is not true, or failure to disclose information, whether or not the representation or disclosure has been warranted to be true and correct, unless that representation or non-disclosure is such as to be likely to have materially affected the assessment of the risk under the policy concerned at the time of its issue or at the time of any renewal or variation thereof.

(b) The representation or non-disclosure shall be regarded as material if a reasonable, prudent person would consider that the particular information constituting the representation or which was not disclosed, as the case may be, should have been correctly disclosed to the short-term insurer so that the insurer could form its own view as to the effect of such information on the assessment of the relevant risk."

The amended wording reads as follows:

"Notwithstanding anything to the contrary contained in a policy, but subject to rule 20.2 —

(i) the policy must not be invalidated;

(ii) the obligation of the insurer under the policy must not be excluded or limited; and

(iii) the obligations of the policyholder must not be increased;

on account of any representation made to the insurer which is not true, or failure to disclose information, whether or not the representation or disclosure has been warranted to be true and correct, unless that representation or non-disclosure is likely to have materially affected the insurer's ability to assess the risk under the policy concerned at the time of the representation or non-disclosure."

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Initially, the wording in the Act did not address the following questions:[167]

- Would its ambit cover non-disclosures?
- What standard would be used for the materiality test?
- Who conducts the assessment of the risk?
- What does materiality relate to?

The area of contention where these concerns were raised, and which related to interpretational challenges, were the claims arena. Claims and complaints are generally the areas where the interpretation of the policy wording is put to the test. In drafting the applicable policy wording, the intention of the drafter is utilized as a baseline. When a claim is lodged, the circumstances of the incident which led to the claim are interpreted against the applicable wording. If a customer has a different view, there would generally be a dispute, resulting in a complaint. The wording would be reviewed in accordance with the complaint to establish if there was a grey area in the policy wording, in effect the possibility for the wording to be interpreted different to its initial intention. If this was the case, the benefit ought to be awarded to the customer. As complaints should ideally be considered by the insurer first, the insurer must deal with these possible interpretational difficulties against the background of the framework discussed *inter alia* in chapter two.[168]

Providing the customer with the benefit under the circumstances discussed above was the intention of the provisions in the Long-Term and Short-Term Insurance Acts.[169] Information provided by customers is very relevant in order for insurers to ensure that the risk is adequately assessed.[170] There is an expectation that any questions posed must be correctly answered.[171] The legislation imposes a duty on customers to disclose facts known to them.[172] The information is generally specific to the risk that is being insured, such as medical information relating to the life being insured, or the customer's occupation or lifestyle.[173] If the incorrect information is provided, it is considered a mis-disclosure and where no information is provided, meaning that there is a lack of an answer, this would constitute a non-disclosure.[174] Both

[167] FSCA *Consultation report and comment matrix – PPRs* 25.

[168] FSCA *Consultation report and comment matrix – PPRs* 25.
[169] O'Connor and Ahmed "The Duty to disclose material information remains" 6 March 2019.
[170] Reinecke and Nienaber "Mis-or Non-Disclosure: Reconstructing the policy" 9 October 2006.
[171] *Ibid.*
[172] *Ibid.*
[173] *Ibid.*
[174] *Ibid.*

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constitute a misrepresentation.[175] Misrepresentations can be positive or negative. A positive misrepresentative is for example where an incorrect response is provided to a question whereas a negative misrepresentation is where there is a failure to disclose material information which is within one's knowledge.[176]

A fraudulent misrepresentation may constitute a delict.[177] Therefore, in order to prove a delict based on misrepresentation, the elements of delict must be proven: conduct, fault, causation, harm and wrongfulness. In the insurance industry, the wrongfulness element has been a source of contention insofar as it concerned the approach to determine wrongfulness in respect of positive or negative misrepresentations, and especially whether a misrepresentation is material.[178] In order for materiality to exist it must, as a matter of probability, affect how the risk was impacted or assessed and it must have altered the manner in which cover would have been provided had the insurer known about the information.[179]

Historically, there were two separate tests which existed to determine materiality: the reasonable insurer under the circumstances and the reasonable insured under the circumstances.[180] The reasonable insurer-test required a review by a prudent and experienced underwriter and, if the underwriter confirmed that the facts would influence his decision, the facts were considered material.[181] The reasonable insured-test considered whether a reasonable insured would regard the facts as relevant to the assessment of the risk.[182]

The legal principles relating to materiality developed in two directions in that there was a subjective and an objective test. The objective test was in respect of negative misrepresentations as evidenced in the case of *Mutual and Federal Insurance Co Ltd v Oudtshoorn Municipality*,[183] where the insurer rejected a claim on the basis of non-disclosure. In this regard, Joubert JA stated that

> "there is a duty on both insured and insurer to disclose to each other prior to conclusion of the contract of insurance every fact relative and material to the risk

[175] *Ibid.*
[176] FSB *Consultation and comment matrix*, *PPRs* 117.
[177] *Tubane v Machakela & Others* [2014] ZAFSHC 193.
[178] FSB *Consultation and comment matrix*, *PPRs* 117.
[179] Reinecke and Nienaber "Mis-or Non-Disclosure: Reconstructing the policy" 9 October 2006.
[180] Dinnie "Reviewing the law on reasonable precautions" 29 January 2020.
[181] *Whyte's Estate v Dominion Insurance Co of SA Ltd* 1945 TPD 382 at 404.
[182] *Fine v The General Accident, Fire & Life Assurance Corporation Ltd* 1915 AD 213 at 220–221.
[183] [1984] ZASCA 129; [1985] 1 All SA 324 (A).

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> or the assessment of the premium. This duty of disclosure relates to material facts of which the parties have actual knowledge or constructive knowledge prior to conclusion of the contract of insurance."[184]

This matter introduced the "reasonable man"-test in respect of which the information which was not disclosed was established to be reasonably relative to the assessment of the risk and premium.[185] The test supported an objective assessment of materiality.[186] However, the case which illustrated the subjective approach is *Qilingile v SA Mutual Life Assurance Society Ltd*,[187] where the court held that the position of the insurer had to be looked at in determining whether a positive representation was material. In keeping with the ongoing interpretation challenges, the Insurance Amendment Act[188] was gazetted with sections 19 and 35 amending sections 53 and 59. The amendments were summarized by Boruchowitz J in *Mahadeo v Dial Direct Insurance Limited*:[189]

> "The effect of the most recent amendment is to bring the law with regard to positive representations into line with the law on non-disclosures. The statutory definition of materiality in section 53(b) is effectively identical to that adopted in the President Versekeringsmaatskappy case in relation to the common law position. The test remains objective: The question whether the particular information ought to have been disclosed is judged not from the point of view of the insurer, or the insured, but from the point of view of the notional reasonable and prudent person. The subjective test propounded in the Qilingile case would appear to no longer apply."

The principle, and scope of application, of materiality have been an ongoing battle within the industry as can be seen from the case of *Jerrier v Outsurance Insurance Company Ltd,*[190] which was heard after TCF became applicable. The clash between materiality and the TCF outcomes was evident in this case.

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[184] *Mutual and Federal Insurance Co Ltd v Oudtshoorn Municipality* at 30.
[185] *Idem* at 29.
[186] *Idem* at 37.
[187] [1993] 1 All SA 324 (A) at 14.
[188] 17 of 2003.
[189] 2008 (4) SA 80 (W) at 7.
[190] 2013 JDR 0562 (KZP).

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The facts were that the insured, as per his motor vehicle insurance policy, was expected to report a claim, or any incident that might lead to a claim, to the insurer as soon as possible but not later than 30 days after the incident. The clause extended to include incidents for which the insured had no intention to claim for under his insurance policy. The insured therefore had a duty to disclose more than the facts which were material in the pre-contractual situation.[191] Based on the facts of the case, the insured had three incidents whilst insured with Outsurance. He had an accident due to hitting a pothole, and a second incident which initially amounted to R 20 000, but which eventually amounted to R 200 000. Upon having his third incident, his claim was rejected on the grounds of him not having disclosed his prior incidents.[192]

The court decided in favour of the insurer. The decision caused widespread panic amongst insured persons because customers were now of the view that they were to disclose all incidents to insurers in the fear of having their claims rejected.[193] National Treasury issued a statement confirming that the then-FSB, Treasury, and the South African Insurance Association (SAIA) were evaluating the impact of the judgment.[194] In this statement, the importance of TCF was stressed once again, and the onus on insurers to ensure that customers understood the limitations and exclusions of the cover that they intended purchasing, were highlighted. The feedback from the meeting was that member companies of SAIA would not reject motor vehicle insurance claims on the basis of minor incidents not having been reported or disclosed by customers.[195]

The matter was taken on appeal in 2015 where the initial decision was overturned.[196] The feedback was in line with the communication from National Treasury to the industry, which stated that insurers could not rely on minor or trivial incidents to reject claims.[197] Chetty J expressed his concern and stated that

> "it can be [difficult] for a prospective client seeking insurance to determine either at the commencement of a contract or at any time thereafter, what a reasonable

[191] FSB *Consultation and comment matrix*, *PPRs* 121.
[192] *Jerrier v Outsurance Insurance Company Ltd* 2013 JDR 0562 (KZP).
[193] *Ibid*.
[194] Treasury "Treasury calls on the insurance sector to be fair to car owners" 4 April 2013.
[195] *Ibid*.
[196] *Jerrier v Outsurance Insurance Company Ltd* 2013 JDR 0562 (KZP).
[197] *Ibid*.

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person would have considered to be material for the purpose of ascertaining the risk to be assumed by the insurer".[198]

The new dispensation supports the strategy that materiality plays a role in ensuring that the TCF principle is upheld and observed by insurers.[199] The intention of the amendments to the Insurance Acts is to ensure that the common law test of materiality applies.[200] However, by removing the wording of a 'reasonable, prudent person' from the Insurance Acts, the subjective test remains relevant.[201] The section allowed for the application of an objective test on representations and non-disclosures. The amended wording is not clear on whether a subjective or objective test should be utilised.[202] The removal of subsection (b) takes us back to the scenario where both tests could be applied.[203] Either of these could be argued, based on the circumstances.[204] The phase "the insurer's ability to assess the risk under the policy concerned at the time of the representation or non-disclosure" allows solely for an interpretation from the perspective of the insurer.[205] This would result in the customer being placed in an unfair position from an onus of proof perspective when attempting to prevent the repudiation of a claim.[206]

The amended wording has further removed certainty regarding the timing of the representation or non-disclosure – especially as far as non-disclosure is concerned because an insured has a duty to inform an insurer of any material change to the risk.[207] The reference to the time of the policy's issue, variation, or renewal was important because it provided a clear indication to an insured when the risk is assessed, and disclosure is required.[208] The proposed amended wording is contrary to the TCF principle of being clear, transparent and concise.[209] Nevertheless, Rule 21.1 of the PPRs makes reference to a reasonable prudent person in an attempt to ensure that the test remains an objective test[210] although the PPRs are categorised as subordinate

[198] *Ibid*.
[199] FSCA *Consultation and comment matrix*, *PPRs* 22.
[200] *Idem* at 87.
[201] *Ibid*.
[202] *Idem* at 121.
[203] *Ibid*.
[204] *Ibid*.
[205] *Ibid*.
[206] *Ibid*.
[207] *Idem* at 87.
[208] *Ibid*.
[209] *Ibid*.
[210] *Ibid*.

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legislation. Based on this contention that was raised, the amendment had reverted to its original state until the alignment of the legislation began.[211]

The matter of *Ganas v Momentum*[212] had also raised controversy within the industry. *Ganas v Momentum* was a claim which was disputed through the offices of the Long-Term Ombudsman. The claim was rejected on the basis of non-disclosure of information considered material during the pre-contractual stage.[213] The facts were as follows: Ganas applied for life cover with Momentum in 2014. He passed away in 2017 and his family lodged a claim. Specific medical questions were posed to Ganas at the application stage in order for Momentum to determine his risk profile. One of the questions was whether he had suffered from "raised blood sugar" and his response was "No". No further information on this point was requested. At the time of claim, it was established that Ganas was tested multiple times for blood sugar levels and his last test was done two weeks prior to the application for cover with Momentum. The results from the last test indicated that he was at risk of raised blood sugar levels in that the test results indicated consistent abnormal high blood sugar levels.

Momentum's underwriters confirmed that, had they been aware of this information at the application stage, the cover would have been declined.[214] It is important to point out that Ganas had not died due to a medical condition, but rather due to an accidental death as he was shot and killed in his home.[215]

The public outcry was in relation to the non-disclosure not being related to the circumstances of Ganas's death.[216] The matter was escalated to the offices of the Ombudsman and the decision on the claim was upheld.[217] The Ombudsman was in agreement with the rejection of the claim with a voidance of the policy from inception and a refund of premiums.[218] The Ombudsman stated that the law was applied to the facts and equity was applied in considering whether a policy would have been issued had the facts discovered at the claims stage been brought to its attention at the time of application for the cover.[219] The Ombudsman, in its feedback, stated

[211] *Ibid*.
[212] Momentum Life "Importance of full disclosure – Momentum shares responses to social media questions on repudiated claim" November 2018.
[213] *Ibid*.
[214] *Ibid*.
[215] *Ibid*.
[216] *Ibid*.
[217] Ombudsman for Long Term Insurance "Matters of Interest – The Momentum/Ganas case" November 2018.
[218] *Ibid*.
[219] *Ibid*.

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that a causal connection existed between the non-disclosure and the conclusion of the contract and not between the non-disclosure and the claim.[220] The rejection was considered sound in that the insurer was misled on the nature and extent of the risk and thus made a decision to accept the policy without full and complete information.[221] Reference was made to section 59 of the Long-Term Insurance Act where it was stated that, if information was regarded as material, the reasonable prudent person would expect that the disclosure of the information to the insurer would allow the insurer to make its own decision as to the evaluation of the risk.

The application of the principles of equity within the office of the ombudsman relating to non-disclosure was that, if in relation to a matter that is not fraudulent, the policy should be reviewed to establish what the policy would have been had there not been a non-disclosure.[222] The office applied the Didcott principle.[223] This principle is defined as "if the insurer would still have issued the policy, albeit at a higher premium – even if the information withheld materially affects the risk to the insurer – then it would not be fair for the insurer to repudiate the claim".[224] In some instances, however, an insurer may establish that the policy would not have been reconstructed as, if the insurer had known the true set of facts, the insurer would not have issued the policy at all. This was the case in the Ganas matter.[225]

Following the concerns raised on Momentum's customer platform, responses from industry and the Long-Term Insurance Ombudsman, the FSCA issued a statement on the matter and highlighted its thoughts on the lessons learned in this case.[226] The challenge with complaints in the public domain is the potential for reputational harm to the brand of the insurer.[227] It was on this basis that Momentum maintained its view on the outcome of the claim but took a business decision to settle the matter with the claimant.[228]

In its communications, the FSCA noted that there is sometimes a disconnect between the customer expectation and the industry feedback.[229] The case provided an opportunity for the FSCA to engage with the industry and move to a position of fairness which builds

[220] *Ibid.*
[221] *Ibid.*
[222] Long Term Ombudsman Rule 1.2.4.
[223] Ombudsman for Long Term Insurance "Matters of Interest – The Momentum/Ganas case" November 2018.
[224] Faurie "When does material non-disclosure void an insurance contract?" 13 August 2013.
[225] Ombudsman for Long Term Insurance "Matters of Interest – The Momentum/Ganas case" November 2018.
[226] FSCA "Statement on the Momentum/Ganas case" 22 November 2018.
[227] *Ibid.*
[228] *Ibid.*
[229] *Ibid.*

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confidence.[230] It supports the FSCA's strategy relating to building confidence in the financial services sector, meaning that customers have a degree of confidence that FSCA's intervention and engagement within the financial services industry will inevitably support better customer outcomes.[231] The FSCA acknowledged Momentum's approach to the case and the fact that same was considered industry practice.[232] The manner in which this matter was handled instilled a degree of confidence within the financial services industry.[233] The FSCA therefore committed to work with the sector to change its practices and promote the interests of customers; to consider whether the regulatory framework specific to underwriting and non-disclosure issues adequately supports fair customer outcomes; and to highlighted a few risks that customers would face if they follow calls to cancel life or investment policies.[234] In my view, this is a fair approach to ensure that there is alignment between the expectations of FSCA versus the delivery of the financial services industry. The fact that the FSCA is in a position to confirm its view and support the industry in clearing any confusion which exists is a step in the right direction.

3.6. Final remarks and conclusion

This chapter built on the structural framework depicted in chapter two and dealt with the substance of the dissertation – complaints management in the insurance industry. I considered the challenges that relate to complaints management and discussed specific changes that the framework set out in chapter two effected to complaints management.

The complaints management framework within the amended PPRs and the provisions within the COFI Bill are intended to provide clarity to financial institutions to ensure consistency and standardization in the process. The intention was to provide certainty to enable the regulation of conduct. The supposed introduction of the principles of fairness, equity and good faith deviated from the principles and strict application of the law of contract. The question that therefore begs to be answered is whether the amendments were now intended to incorporate these common law principles and public policy into the legislative regime.

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[230] *Ibid.*
[231] FSCA *Regulatory Strategy* 57.
[232] FSCA "Statement on the Momentum/Ganas case" 22 November 2018.
[233] *Ibid.*
[234] *Ibid.*

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This discussion links with the equity considerations that form part of the discussion in chapter four. Chapter four deals with complaints handling within the insurance industry specific to the various ombudsman schemes. It sets out the principles by which the financial services industry abides by in relation to equity and materiality to ensure fair customer outcomes. It considers the existing structure and highlights the need for a change to ensure standardized and consistent processes.

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Chapter 4: The complaints management framework in South Africa, specific to the ombudsmen schemes

4.1. Introduction

This chapter deals with complaints handling within the insurance industry specific to the various ombudsman schemes. It sets out the principles by which the financial services industry abides by in relation to equity and materiality to ensure fair customer outcomes. It sets out the existing structure and highlights the need for a change to ensure standardized and consistent processes.

4.2. Background

The focus has thus far been on the TCF framework, the implementation of TCF, the measures which the FSCA will utilize to detect, monitor and deal with TCF compliance and the manner in which it would deter unfair treatment of customers.[1] However, in order to ensure that there is ongoing monitoring of market conduct outcomes, support structures are necessary. The FSCA acknowledges that, regardless of how stringent and comprehensive the regulatory frameworks are, there is always room for abuse.[2] There will be customers who are subject to unfair treatment by financial institutions.[3] It is therefore of importance for customers to have access to simple and effective alternative dispute resolution mechanisms.[4]

The FSOS Act makes provision for statutory and voluntary ombud schemes.[5] An ombud is an alternative channel of escalation, which is generally free to a customer.[6] Whilst the customers are not compelled to make use of the scheme, it does serve as an option to litigation.[7] The customer is not bound by the decision of an ombud scheme; however a financial institution is.[8]

These schemes have assisted the FSCA to confirm whether there has been unfair treatment of customers within the financial services industry.[9] The commitment and need to drive the financial sector to serve South Africans better, requires an effective, streamlined, and

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[1] FSB *TCF Road Map* 29.
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] *Ibid.*
[6] Treasury *Draft Market Conduct Paper* 57.
[7] *Ibid.*
[8] *Ibid.*
[9] FSB *TCF Road Map* 29.

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consistent ombud scheme.[10] The ombud schemes will continue to support the FSCA in carrying out pre-emptive supervision at an industry and financial institution specific level.[11] These schemes will need to be in sync with the FSCA from the perspective of its monitoring findings, the development of the regulatory framework, and TCF, to ensure that they are in a position to recognize abuse and breaches of TCF practices.[12]

It has been established, through various studies and reviews, that seventy percent of complaints within the insurance industry are based on long- and short-term insurance policies.[13] Based on these statistics, there have been ongoing initiatives to strengthen the oversight on market conduct concerns as identified by the various ombud schemes.[14] The current schemes have provided great insight into complaints, and identified trends and potential risks from a market conduct perspective, but these initiatives have taken place by way of a silo approach.[15]

There have been challenges in co-ordination, transparency and the ability to ensure co-ordination amongst the various ombud schemes.[16] From a customer perspective, it could be challenging and difficult to ensure that the correct ombud scheme is approached for assistance.[17] The jurisdictional boundaries also make it difficult to establish which ombud is most appropriate for the type of complaint which is being lodged.[18]

In light of the above, it is clear that the current set of schemes do not align with the vision of a well-developed system as there are currently six different schemes which differ in how they are established and how they operate.[19] The aims of these ombud schemes are consistent in that they have been set up to help and support financial customers, however, there have been inconsistencies, weaknesses, and inefficiencies in the manner in which they operate.[20] These shortcomings hinder the achievement of good customer outcomes.[21]

It is important to understand the purpose of a financial ombudsman within the financial sector. Such a body is a forum considered as a form of alternative dispute resolution. An ombudsman

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[10] Treasury *A known and trusted ombud system for all* 18.
[11] FSB *TCF Road Map* 29.
[12] *Ibid.*
[13] Treasury *A known and trusted ombud system for all* 1.
[14] *Ibid.*
[15] *Ibid.*
[16] Treasury *Draft Market Conduct Paper* 57.
[17] *Ibid.*
[18] *Ibid.*
[19] Treasury *A known and trusted ombud system for all* 1.
[20] *Ibid.*
[21] *Ibid.*

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is intended to investigate and resolve complaints brought by customers.[22] The process aims to resolve customer complaints with little or no cost to the customer, as opposed to litigation which is a lengthy and expensive process.[23] The offices of the ombudsman also deal with queries and report on the complaints which they handle. The purpose of the reporting is for the industry to identify trends and analyse the shortcomings identified for corrective action to be taken.[24] This aligns with the regulatory dispensation to ensure better outcomes for financial customers.

4.3. An overview of the challenges relating to complaints handling practices by ombudman schemes

Customers, at times, approach the Regulator directly with regard to their complaints. Whilst this is not unacceptable, it does raise some questions. First, whether a customer is aware of a firm's internal complaint handling practices, and what the reasons are if the customer is unaware of these avenues. Second, whether the customer elected to contact the Regulator directly due to frustration with the levels of escalations available, such as internal escalations and ombudsman schemes.

Whilst the Regulator would receive complaints from a customer, I have already indicated that the regulatory body does not adjudicate the dispute save in limited instances. The preference is for an ombud scheme to handle the matter because the ombud should have the ability to review a complaint based on fairness, taking into consideration the policy as well as the provisions of the law.[25] An ombud has more flexibility compared to a regulator, who is also responsible for oversight and punitive action. The regulator's powers are restrictive in that it usually functions with limited resources, which inhibits the ability to deal with each and every individual customer complaint.[26]

Regulators are generally equipped to take action based on any transgression of the law. I acknowledge that may not be in line with the new regulatory dispensation and the intentions behind TCF, but the Regulator would be in a position to track and monitor trends relating to complaints which its office receives directly. This is essentially the conceptual distinction

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[22] *Idem* at 3.
[23] *Ibid.*
[24] *Idem* at 11.
[25] *Ibid.*
[26] Treasury *A known and trusted ombud system for all* 11.

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between a regulator and an ombud scheme.[27] Regulators have the capability to engage with financial institutions to understand the nature of transgressions and provide a directive to remedy identified transgressions which benefit not only an individual complainant, but those who may be similarly affected. Ombud schemes, on the other hand, are limited to the individual complaints.[28] Despite this being seen as a limitation, the ombud schemes do publish data and detail relating to certain outcomes of complaints. An example is that of the Ganas/Momentum matter mentioned above. The purpose of the publications is to share information so the rest of the financial services industry can understand the concepts reviewed and align with the expectations of the ombud scheme as well as that of the Regulator.[29] Another consequence of such a publication would be the publication of detail pertaining to insurers who do not practice fair outcomes to customers. Such publications receive reviews within the public domain and attract negative publicity from a marketing perspective.[30] In my view, the publication of information and data would be a value add to the industry in that in its current state, information is published on a limited basis. It is therefore difficult to benchmark against institutions and establish a best practice. The negative connotation is the context relating to publications. Whilst there is great value, without adequate context relating to the information, which is published, there is room for error in terms of interpretation and analysis.

A grave challenge is the cumbersome, and sometimes confusing, process relating to the re-directing of customer complaints.[31] There are complaints where various ombud schemes could be involved due to the nature and complexity of the case.[32] This may result in a complainant and a financial institution having to deal with several ombuds. The credibility of the process and its fairness may come into question.[33] This would likely result in a customer no longer trusting that the ombud process is a fair and reasonable one. This would result in time delays and several sets of feedback for a customer and financial institution from various ombuds.[34] This could also result in a frustrated and confused customer as each ombud scheme would have its own process, timelines, and communication methodologies.[35]

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[27] *Ibid*.
[28] *Ibid*.
[29] FSB *TCF Road Map* 28.
[30] *Ibid*.
[31] Treasury *A known and trusted ombud system for all* 11.
[32] *Ibid*.
[33] *Ibid*.
[34] *Ibid*.
[35] *Ibid*.

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There is an expectation on financial institutions to meet certain legal requirements which extend to include customer needs and expectations. The ombuds schemes provide an external channel for recourse to the customer in the event of a breach. In South Africa, there are several channels for such recourse, which include internal dispute resolution processes within the financial institution; voluntary or recognized ombudsmen; statutory ombudsmen or adjudicators; industry associations that handle consumer complaints; sector regulators that handle consumer complaints; the Department of Trade and Industry; provincial consumer offices; courts and civil society e.g. debt counsellors, non-profit attorneys.[36] These channels should support the strategy of better protection of customers.[37] The purpose of the channels should be clearly set out to ensure that a customer understands its purpose and that multiple channels are not accessed to try to obtain a favourable outcome to the complaint.[38] There should therefore be standardization of approach and principle relating to how these channels are accessed and what they are intended to achieve.[39]

South Africa has two sets of ombud schemes. The first set refers to those established by statute where the ombud derives its powers from legislation.[40] The second set refers to a voluntary ombud scheme which is brought into power to serve a specific financial industry segment, for example, an ombud set up by long-term insurers to deal with long-term insurance customer disputes.[41] In 2007, a FinMark Trust report recommended changes to the alternative dispute resolution structure of the South African environment in order to promote the fair treatment of its financial customers.[42] Several positive outcomes were identified within the current system; however, changes were recommended to allow for ease of access and understanding for customers, and to provide clear direction to measure the impact of changes.[43] These current structures are being evaluated to establish the structure from a best practice perspective. The element of cost would also need to be considered to establish what would be best suited, considering the variation in the customer base of the financial services industry.

Whilst the ombud schemes have operated independently, they have satisfied the overarching aim of ensuring that customers had access to a dispute resolution channel which supported

[36] *Idem* at 9.
[37] *Idem* at 3.
[38] *Ibid*.
[39] *Ibid*.
[40] *Idem* at 19.
[41] *Ibid*.
[42] Finmark *Trust Landscape for Consumer Recourse in South Africa's Financial Services Sector* November 2007.
[43] Treasury *A known and trusted ombud system for all* 9.

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impartiality, fairness and equity.[44] The schemes were also accessible by all customers and although the approaches differed, they satisfied the need of the customer from the perspective of having a channel of escalation for complaints.[45]

The FSRA changed the ombud system as there were (and still are) several challenges which inhibit the effectiveness of the system. The first issue relates to the number of complaints received in relation to the market base, which may be a reflection of level of awareness of the ombud system and the customers' ability to access same.[46] Customers nevertheless appear to be confused about the role of the various ombuds and their respective jurisdictions.[47] This was identified in the trends relating to queries received by the various schemes and illustrates the lack of understanding of the existence, purpose, and functions of the various ombuds.[48]

The second issue relates to shortcomings in coverage and jurisdictional inefficiencies.[49] Unfortunately, the ombud offices are not located with each region or province and this denies access to many customers.[50] The other aspect which poses concerns are the jurisdictional inefficiencies where the scheme does not have jurisdiction.[51] Unlicensed entities such as funeral parlors fall outside the framework. When customers buy funeral insurance from an unlicensed entity, the Regulator cannot provide any guarantee or oversight in terms of the manner in which the policy was sold or the manner in which the benefits are considered.[52] The ombud schemes also have no jurisdiction to support the customer when a complaint is lodged.[53]

Those financial institutions which do not subscribe to voluntary schemes are also not subject to the process. These complaints could be referred to the statutory ombud, however, this is dependent on the customer being aware of the process and, if received by a voluntary scheme, the complaint be directed accordingly. This becomes a time consuming and cumbersome process, which results in the inefficiencies related to the resolution of disputes.[54]

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[44] Treasury *Twin Peaks in SA: Response & Explanatory Document* 44.
[45] *Ibid*.
[46] Treasury *A known and trusted ombud system for all* 19.
[47] *Ibid*.
[48] *Ibid*.
[49] *Ibid*.
[50] *Ibid*.
[51] *Ibid*.
[52] Mudau "*Why must funeral policies be underwritten by an insurer*" 16 April 2021.
[53] *Ibid*.
[54] Treasury *A known and trusted ombud system for all* 19.

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4.4. Reform of ombud schemes

The FSRA makes provision for an Ombud Council to replace the FSOS Council.[55] The FSRA enhances the FSOS Act, which will be repealed to strengthen the role and powers of the FSOS Council.[56] The FSOS Council will therefore be a statutory body to allow for a single point of entry into the ombud schemes.[57] As of 1 November 2020, the ombud system was to be overseen by the new Ombud Council.[58] It also changes the current subscribing mechanisms whereby a financial institution can elect to be a part of the scheme.[59] In future, all registered financial institutions will be a part of the ombud schemes. All voluntary ombuds will also fall within the ambit of the Council.[60] This Council will be required to promote the awareness, accessibility and use of the ombud system.[61] It is intended to enhance the efficiency of the system and impose consistency in terms of its operation.[62] Where there is confusion or uncertainty relating to jurisdiction, the Ombud Council is empowered to resolve and determine which Ombud will be responsible for hearing the matter.[63] The FSRA now provides for the following:

- An appropriate ombud scheme to cover all financial products;
- The requirement for all financial institutions to be a member of an industry ombud scheme;
- Powers of the Ombud Council to establish which ombud would be best suited to a case where no voluntary ombud is available;
- Enhanced powers of the Council and a mandate for improvement of the ombud system;
- Appointment of a Chief Ombud;
- Streamlined and enhanced governance structures with clear guidelines relating to accountability – the aim is to develop a framework for external dispute resolution mechanisms that is known for consistency approaches;[64]
- The requirement for all ombuds to consider fairness and equity in their processes of evaluation of complaints, whilst taking into consideration the law of contract;
- An appeal mechanism to the Financial Services Tribunal established in terms of the Act;

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[55] *Ibid*.
[56] *Ibid*.
[57] Treasury *Twin Peaks in SA: Response & Explanatory Document* 44.
[58] World Bank Group *South Africa Financial Ombud System Diagnostic* 35.
[59] Treasury *Twin Peaks in SA: Response & Explanatory Document* 44.
[60] *Ibid*.
[61] Treasury *A known and trusted ombud system for all* 19.
[62] *Ibid*.
[63] *Ibid*.
[64] *Ibid*.

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- A single point of entry into the ombud system; and
- A clear distinction between the Ombuds, the council and the FSCA with regard to roles, responsibilities and the respective structures.[65]

The criteria set out above attempt to solve some of the historic challenges relating to the general lack of knowledge by customers of the nature and manner of operation of an ombud scheme; inadequate transparency and accountability of ombuds; jurisdictional issues of the various ombuds and the resultant confusion of customers; and the need for greater co-ordination and consistency among ombud schemes.[66]

Given the above context relating to the various ombud schemes and the way forward, it is important to reflect on the historic decisions made by the schemes and to understand the context relating to some of these decisions. There have been several instances where the ombud scheme did not agree with the decision made by the insurer which resulted in an overturn of the insurer's finding. It is also important to reflect on these decisions as some overturns are not specifically based on an interpretation of the policy and/or contract. They are equity-based decisions.[67] Some of these decisions are referred to below in order to illustrate this practice.

As an interjection, a brief overview of the process discussed earlier.[68] A customer that is dissatisfied with a decision relating to a financial product or service approaches the financial provider. The customer lodges a complaint, and the insurer reviews the objection based on its internal policies, taking into consideration what the product or service policy/contract determines. In this regard, the definitions of "complaint", "query" and "complainant" are relevant[69] to determine (in line with the legislation) how the insurer should deal with the matter. Interwoven, and not necessarily dependent on these definitions, is the corporate-wide necessity to comply with TCF and treat the customer fairly.[70] Provision is made for a consumer to be compensated for unlawful behaviour. In addition to the above, the insurer may also decide to assist the consumer notwithstanding a policy/contract-based obligation to do so. In this regard, the following definitions are relevant:

[65] *Ibid*.
[66] *Ibid*.
[67] World Bank Group *South Africa Financial Ombud System Diagnostic* 50.
[68] See par 3.3. above.
[69] *Ibid.*
[70] See paras 2.4.4 and 3.5 above.

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> "'Goodwill payment' means a payment by a financial institution to a complainant as an expression of goodwill aimed at resolving a complaint, but where the financial institution does not accept liability for any financial loss to the customer as a result of the matter complained about."[71]

> "'Compensation payment' means a payment, other than a goodwill payment, by a financial institution to a complainant to compensate the complainant for a proven or estimated financial loss incurred as a result of the financial institution's contravention, non-compliance, action, failure to act, or unfair treatment forming the basis of the complaint, where the financial institution accepts liability for having caused the loss concerned."[72]

> "'Compensation payment' excludes –
> (c) payment of amounts contractually due to the complainant in terms of the financial product or service concerned, or
> (d) refunds of amounts paid by or on behalf of the complainant to the financial institution where such payments were not contractually due but includes interest on late payment of amounts or refunds referred to in (a) or (b)."[73]

Should the customer not be satisfied with the outcome of the insurer's internal processes, the ombuds may be approached – a fact of which insurers are all too aware. The manner in which ombuds determine outcomes on an equity basis differs, often preventing a financial institution from understanding how to rectify their process or service to ensure that customers receive a standardized and aligned offering.[74] In this regard, the substance of the complaints management process – its design and review – become dependent on these considerations. Financial institutions, at times accept a prior ruling to avoid a further adverse finding by the ombud.[75] In my opinion, this is an inherent flaw insofar as customers that manage to approach an ombud may ultimately end up in a better position that a customer that accepted the finding, and reasons provided for the finding, of the insurer.

[71] FSB *TCF complaints management* 3.
[72] *Ibid.*
[73] *Ibid.*
[74] *Ibid.*
[75] *Ibid.*

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A further discrepancy is that the processes and rules, depending on the ombud scheme being dealt with differ from the perspective of timeframes, accessibility of decisions, differing levels of public reporting, different levels and mechanisms for engagement, lack of specialist or industry knowledge.[76] In light of the above, there are three models which are currently under consideration: a hybrid model building on the current FSRA provisions; a centralized model establishing a single statutory ombud scheme, and an industry ombud scheme with strong oversight by the Ombud Council.[77] The key themes which are highlighted across the proposals are the concerns relating to specialist skill being lost; further challenges with efficiency and jurisdiction; whether customer confusion would be reduced; would the theme of consistency in process be prevalent; flexibility of the system to cope with future regulatory changes.[78] There are areas for improvement and these would extend to include: broadening the scope of products and services which the ombud schemes have jurisdiction over; ensure that there are clear guidelines relating to jurisdiction; consistent and standard processes for handling of complaints; aligning definitions; clear timelines for submission of complaints and standardized processes for reviewing jurisdiction in terms of timelines.[79] Recommendations are that the structures be reviewed in conjunction with advantages and disadvantages to establish a new model that would best suit the South African context.[80]

However, even though there are proposal for reform of the schemes, it still does not address the misalignment between the ombud scheme and the insurance industry where ombuds decisions (which are binding on insurers) are based on equity and fairness. This may be ameliorated by a proper uptake of TCF by the industry,[81] provided that what the FSCA, insurance industry and ombuds view as "fair" align.

4.5. Long-term Insurance Ombudsman determinations illustrating equity-based decisions

4.5.1. Introduction

The ombud schemes have been renowned for applying equity and fairness in their decision-making.[82] This application reduces certainty in terms of policy interpretation and application.[83]

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[76] *Ibid*.
[77] *Idem* at 52.
[78] *Idem* at 50.
[79] *Idem* at 70.
[80] *Idem* at 161.
[81] Stokes "Where principles of equity and fairness hold sway over policy wordings" 23 June 2020.
[82] *Ibid*.
[83] *Ibid*.

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The principle of equity and fairness is intended to support the delivery of the TCF outcomes as opposed to the strict application of contract law.[84] The scenarios set out below are anticipated to demonstrate the view relating to equity-based decisions.

4.5.2. Case 28

An application for a funeral policy was made on 11 December 2011, wherein the name of the deceased was listed under the heading "Children". A claim was lodged upon the death of the child. The child was the biological child of the claimant's sister. The claimant had lodged a claim under the "immediate family benefit" which provided cover for "your own, step or legally adopted unmarried child who is younger than 21". The claimant's case was based on the submission that the deceased was his legally adopted child.

The insurer denied the claim on the basis of premium prejudice having been suffered because it would have offered cover under an extended benefit with an additional premium. An extended benefit would be a benefit afforded to an individual other than the principal life being insured. The claimant refused to accept the decision that the child being claimed for was not considered the child of the claimant and argued that, by customary law, the adoption was legally enforceable. The Long-Term Ombudsman made a provisional ruling upon evaluating the complaint wherein the insurer was requested to pay the claim in full. The insurer disputed the ruling on the basis that the customary adoption did not satisfy the requirements of an adoption in terms of the Children's Act 38 of 2005 and noted that the complaint ought to be dealt with by a court. The office of the ombudsman conceded to the fact that there existed a dispute of fact relating to the legality of the customary adoption. The insurer argued against the jurisdiction of the offices of the Ombudsman and was of the view that a court should make a decision on the legality of the adoption. The insurer refused to attend a meeting with the Ombudsman and the complainant to discuss the circumstances of the complaint and the decision which was reached by the Ombudsman.

The ombudsman, in consideration and application of its rules, considered the following matters with regard to the insurer's reliance on litigation to resolve the issue:

- The amount being claimed in relation to the cost of litigation, the expense and delay of a legal process, was not justified;

[84] *Ibid.*

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- The geographical location of the complainant and his witnesses (rural area) in relation to where the insurer conducts its business (Gauteng), as litigation would favour the insurer from a logistical perspective; and
- The insurer's failure to attend a meeting which could have addressed its concerns/issues surrounding the clarity which it sought through a legal process.[85]

The offices of the ombudsman held an adjudicator's meeting wherein a decision was taken that the complainant had satisfied the office that evidence put forth relating to the customary adoption would satisfy the requirements to meet the legality thereof. The issue which remained unresolved was the definition of "legally adopted child" and the insurer argued that this debate could only be resolved by a court of law.

The ombudsman stated that it had jurisdiction to make an award on a "…balance of probabilities and with due regard to the incident of onus". A strict interpretation of the policy was not applied. The circumstances were looked at and a decision was reached that the complainant had allegedly failed to comply with the customary law requirements for a valid customary adoption. The complainant was not in a position to provide documentary proof of the adoption. However, in all probability and based on the evidence submitted by the complainant, the adoption was considered legal. The insurer was ordered to pay the claim. Whilst the insurer did not agree with the decision, upon weighing its options, the claim was settled in full on an ex-gratia basis. The ruling was in favour of the complainant and the settlement was considered a settlement in terms of the policy. However, the insurer for its own record-keeping, elected to settle same on an ex-gratia basis.

4.5.3. Case 34

This matter was a claim under a funeral benefit for a wider family member, which was declined.[86] The deceased was insured as the complainant's cousin. The policy wording defined "cousin" as "[a] [c]ousin who is the child of the policyholder's aunt or uncle". At the claims stage, it was established that the deceased was the second cousin of the complainant and therefore the complainant did not meet the requirements for a successful claim. The insurer stated that the onus rested on the complainant to disclose the correct information at policy inception and, since this was not done, there were no meeting of the minds. The insurer was of

[85] Case 28, available at https://www.ombud.co.za/useful-information/final-determinations.
[86] Case 34, available at https://www.ombud.co.za/useful-information/final-determinations.

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the view that the complainant failed to disclose the relationship correctly as it did not meet the definition of "cousin" in terms of scope of cover that the insurer offered. The premiums in respect of cover for the deceased's insured life were refunded. The complainant raised the fact that he had contributed toward the funeral of the deceased.

The offices of the ombudsman stated that, in terms of contract, the insurer was correct in its application. However, it had to be noted that, in certain cultures, the reference to a "cousin" could include a second cousin. After the claim, the insurer conducted research and effected a change to policy wordings for future customers. The ombudsman stated that this could be viewed as an acknowledgement by the insurer of the need to expand its definition of "cousin" to cover a wider network of family. The ombudsman further stated that, from the point of view of a reasonable person in the same set of circumstances as the complainant, there was an expectation that an individual whom he thought of as a cousin would be covered in terms of the policy. From an equity and fairness perspective, the ombudsman issued a ruling requesting that the insurer pay the claim. It was established that:

- The reference to "cousin" in the culture of the complainant extended to his wider family network;
- The understanding of "cousin", and the intention when the policy was taken, was to extend to the complainant's wider family network;
- Taking into consideration the culture of the complainant, this was a reasonable expectation;
- Based on the fact that the insurer sold the product to this specific market segment, the research and trend analysis should have been done earlier to align with the expectation of its market; and
- The insurer researched the trends within the market following the claim and this was an indication of a potential disconnect between the insurer's intention and the expectation of the market to which it sold its product.

The insurer acknowledged the feedback from the ombudsman and settled the claim accordingly.

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4.6. Final remarks and conclusion

What can be established by looking at the fairness and equity decisions by the offices of the ombud is that, while some matters fall within the strict ambit of the policy and/or contract, they do not necessarily support fair outcomes for the customer based on the latter's needs, intentions or understanding when entering into the contract.[87] Various factors are reviewed when reaching such decisions which inevitably justify the fair treatment of the customer and which support the ethos of TCF. The changes brought about by the Regulator within the boundaries of the PPRs are a clear indication of how matters are to be evaluated by insurers as well as regulatory bodies. Where there is misalignment in terms of the intention of the application of the policy wording versus the circumstances of the incident when a claim is submitted, an insurer ought to give the benefit of interpretation to its customer. It should not simply repudiate a claim.

The PPRs now make the role of the insurer clear and the new PPRs are closely aligned with the TCF outcomes-based framework. The subordinate legislation and regulatory requirements demand that all stakeholders must demonstrate that customers are treated fairly.[88] What is of importance to note is the fact that an insurer is ultimately responsible to ensure that the legislative and regulatory provisions are adhered to.[89]

Fairness was a defence which was utilized to introduce various "equitable doctrines".[90] The concept of TCF adds a new perspective to the viewing of contracts. Providing incorrect advice at the onset affects the terms and conditions of the contract. Of importance and specific to the ombudsman schemes (long-term and short-term) is the fact that the cases are not considered precedent setting. These are also not published, therefore making it difficult to analyse and establish whether fairness exists. The decisions of the long-term and short-term ombudsman are not considered precedent setting due to the jurisdiction in terms of equity. A question then arises, as to whether this should be considered part of the change.

This chapter dealt with the ombudsman schemes. The components that were addressed were the decisions, consistency, equity and fairness considerations in the decisions and what constituted materiality. It was found that there is a need for change within the sector and that a

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[87] FSCA *Proposed amendments to the PPR made under the LTIA & STIA, consultation report* 7.
[88] FSCA *Consultation and comment matrix PPRs* 2.
[89] FSB *TCF complaints management* 12.
[90] Millard (2014) "Through the Looking Glass: Fairness in Insurance Contracts – A caucus race?" *THRHR* 551.

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review will be done to address same. The initial phase was the amalgamation of the offices of the long-term and short-term ombudsman.

The next chapter deals with reporting and its relevance to complaints management. The ombudsman schemes were the initiators of reporting relating to complaints management. These offices set the benchmark relating to publication of industry statistics and an understanding of what market conduct indicators were and how financial services customers were impacted.

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Chapter 5: Reporting and its relevance to complaints management

5.1. Introduction

Reporting is intended to provide an early warning to the FSCA and supervisors of potential or existing conduct risks. The early detection is intended to support the industry in averting these risks by taking remedial and preventative action to ensure that customers do not encounter unfair treatment.[1] It would also be a mechanism for financial institutions to identify positive behaviours and areas where they are able to improve customer outcomes.[2] Complaints reporting to the Regulator has therefore become necessary for the risk-based approach to be effective.[3] A financial institution's complaints management process would establish its reporting capability and set out the guidelines to ensure that same is effective.[4]

The regulatory and supervisory approach requires that the FSCA be in a position to proactively identify conduct risks and trends.[5] The regulation imposes an obligation on the FSCA to ensure that financial institutions are delivering fair outcomes to their customer base and further that the FSCA is in a position to review and identify risks and to ensure that there are steps to mitigate unfair customer outcomes.[6] This entails focused research and analytic capabilities. The area which has focus on complaints is data and its analysis. This would be done through reporting mechanisms, such as through statutory returns or other data sets enabling the FSCA to monitor market conduct risk.[7]

This chapter deals with aspects of reporting and what the expected outcomes of reporting should be. Reporting has always been considered from a financial perspective. However, there are aspects of reporting which should be looked at to determine whether any market conduct risk exists, its severity and whether any action would be warranted.

5.2. Background

FSCA, in conjunction with the insurance industry, has developed a quarterly reporting tool, which establishes the mechanism to comply with reporting requirements.[8] As reporting on

[1] FSB *TCF complaints management* 16.
[2] *Ibid.*
[3] *Ibid.*
[4] *Idem* at 8.
[5] FSCA *Regulatory Strategy* 29.
[6] Section 58(1) of the FSRA.
[7] FSCA *Regulatory Strategy* 29.
[8] FSB *CBR's Revised Categorisation* 2.

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complaints management also features in the reporting tool, it allow for the strategy relating to reporting to be fulfilled.[9] Its intended purpose is to identify trends, root causes for complaints, and areas for improvement relating to products sold or services rendered to financial customers.[10]

The historic manner of reporting was for purposes of compliance and to ensure that the reporting requirements in terms of regulatory requirements were met. Since the launch of CBRs, an analysis on complaints is expected to be done with the intention of identifying common root causes of problems in the industry, a failure in systems or processes, detection of poor staff or service provider performance, and tracking success.[11]

As financial institutions benchmark their effectiveness against TCF outcomes that the FSCA also uses to determine its success relating to its regulatory and supervisory approach,[12] financial institutions and the FSCA should be in a position to establish whether TCF outcomes are being adhered to. In order to be in a position to do so, complaints should be categorised into the TCF categories.[13] The reporting in terms of CBR's is aligned to the categorisation of complaints per TCF.[14]

It is important to note that the categorisation in accordance with TCF is a guideline. Financial institutions should provide as much detail as possible in order for complaints data to be utilised in an effective manner.[15] The level of reporting is not limited only to the complaints which are received by the financial institution from the customer. It extends to include complaints which the financial institution receives from the various ombud schemes.[16] Financial institutions are expected to analyse the complaints which they receive from the ombud and monitor determinations with a commitment to understand risks in their own processes, products and service.[17]

The FSCA utilises the data to monitor, track and request feedback from financial institutions where poor customer outcomes are noted.[18] The constant and consistent expectation is that

[9] FSB *TCF complaints management* 16.
[10] FSB *CBR's Revised Categorisation* 2.
[11] FSB *TCF complaints management* 10.
[12] *Ibid.*
[13] *Ibid.*
[14] FSB *CBR's Revised Categorisation* 2.
[15] FSB *TCF complaints management* 10.
[16] *Ibid.*
[17] *Ibid.*
[18] *Idem* at 16.

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complaints data be submitted in a format, and with information, in a manner in which it can be used.[19] The data would also be utilised to establish which financial institutions require greater scrutiny and which should be prioritised from the perspective of a principles and risk based supervision.[20] In order for the FSCA to be enabled in terms of analysing, responding and being effective in its decision making, it would require comprehensive reporting.[21]

The Regulator had envisaged public and non-public reporting wherein financial institutions could likely be expected to disclose statistics relating to claims reporting which would include repudiations, timelines, disputes as well as complaint statistics which included adherence to service levels, responses and complaint volumes.[22] The intention behind public disclosure is to establish fair and meaningful information to allow financial institutions and customers to utilise to compare.[23] The public disclosure would also serve the purpose of a deterrent of unfair customer outcomes.[24] Whilst public disclosure has the intention of leading to fair and meaningful comparisons between financial institutions, it is necessary to ensure that financial institutions are compared with others who operate in the same sphere with the same level of complexity in terms of model and product and service offering.[25] The intention of public disclosure is to assist in support of competitive advantage from the perspective of improved perceptions from the public.[26] Non-public reporting will also be looked at from the perspective of granular detail being requested by the FSCA in order to understand whether the financial institutions commit and adhere to the TCF principles which have become entrenched into regulation.[27]

5.2. Reports which are published and the story they tell

Historically, the ombudsman for short-term insurance and long-term insurance published an annual report. The annual report detailed the statistics of the complaints that each office had dealt with during the course of the year. Each report sets the expectation in terms of reporting on complaints, an analysis of complaints data, and the granular level of detail which it is expected to have. This part provides details relating to the complaints which are reported on

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[19] *Ibid.*
[20] *Ibid.*
[21] FSB *TCF Road Map* 24.
[22] *Ibid.*
[23] *Ibid.*
[24] *Ibid.*
[25] *Ibid.*
[26] *Ibid.*
[27] *Ibid.*

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by the short-and-long term ombudsman as well as their analysis and feedback to the insurance industry relating to the data. 2018 was selected as the period for discussion on reported cases as the ombud schemes had aligned to the FSCA requirements for complaints management specific to the TCF categories as well as root cause analysis.

In terms of short-term insurance complaints which were received in 2018, the ombudsman for short term insurance (OSTI) confirmed that the make-up of finalised complaints was as follows: 48% related to motor vehicle insurance, 21% to homeowners, 9% commercial insurance, and 5% household contents insurance. Seventeen percentage of complaints making up the balance related to insurance products such as personal accident, water loss, travel, devices, legal expenses as well as hospital and gap type policies.[28] An analysis of the complaint statistics revealed that the customer complaints were generally in relation to repudiation disputes, in effect a customer disputing the outcome of a claim.[29] This further allude to customers potentially not understanding the terms and conditions of their policy.[30]

OSTI investigates a received complaint by requesting the relevant sales calls and policy documentation in order to understand what the feedback to the customer was, and the position when the policy was sold.[31] Upon investigation and review, and should OSTI be satisfied that the financial institution has satisfied the regulatory requirements in terms of disclosures and fair and transparent processes, OSTI would not be in a position to fault the decision of the insurer.[32]

The complaints are further analysed to establish what, in these particular categories, these customers complained about the most.[33] During 2018, the majority of the vehicle-related complaints considered by OSTI were in relation to accidental damage. Further categories of complaints under this section were in relation to warranty, mechanical breakdown, theft, and hijacking.[34] Upon an analysis of the reason for the complaints, it was established that customers disputed the settlement on claims and reached out to OSTI to arbitrate.[35] These disputes ranged from the calculation of the offer to settle, salvage values, to credit short-falls.[36] Complaints

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[28] OSTI *Annual Report 2018* 21.
[29] *Ibid.*
[30] *Ibid.*
[31] *Ibid.*
[32] *Ibid.*
[33] *Ibid.*
[34] *Ibid.*
[35] *Ibid.*
[36] *Ibid.*

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relating to outcome or repudiation disputes were in respect of non-disclosure on the part of the customer, or misrepresentation of information when the policy was being sold.[37] OSTI, in its analysis, established that 18% of the claims which were referred under the motor category were resolved in favour of the customer.[38]

In terms of the category relating to homeowners, OSTI received complaints relating to claims where damage was caused to property due to storm related incidents.[39] Most of these complaints were in relation to repudiation disputes due to the condition of the property, ie claims were excluded due to the property not being maintained and the damage having been caused due to a lack of maintenance.[40]

Financial institutions are expected to analyse their own data in this regard to establish how (and whether) to change this behaviour from the perspective of service, process, or decision-making.[41] In essence, there is an expectation that financial institutions understand why customers elect to refer their disputes to an external party, the OSTI, as opposed to the financial institution. The customer may not feel secure that the financial institution is adequately equipped from a process perspective, or the view is held that the OSTI provides an independent and impartial process.

The OSTI further analyses the overturn ratio, in effect the number of complaints resolved in favour of the insured in relation to the number of complaints finalised. The overturn ratio is an indicator for a financial institution as well as the FSCA of market conduct concerns. It does not imply that the financial institution is not treating its customers fairly, it is an indicator for the financial institution and the FSCA to investigate further to gain an understanding of why a financial institution's customers elect to approach the OSTI as a complaint escalation.[42] It is also an indicator that an insurer is co-operating with the office of the ombudsman, in that it is agreeable to its processes.[43]

The Ombudsman for Long Term Insurance (OLTI) has historically published statistics that differ from that published by the OSTI. The OLTI has differing levels of complaints which are

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[37] *Ibid.*
[38] *Ibid.*
[39] *Ibid.*
[40] *Idem* at 22.
[41] *Idem* at 21.
[42] *Ibid.*
[43] *Ibid.*

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received, based on its involvement in those cases.[44] The categories of complaints which the OLTI receives are credit life, funeral, disability, health, and life.[45] The OLTI categorises its complaints into the following further sub-categories to provide an understanding of the types of complaints handled by the office: "poor communications/documents or information not supplied/poor service", "claims declined (policy terms or conditions not recognised or met", "claims declined (non-disclosure)", "dissatisfaction with policy performance and maturity values", "dissatisfaction with surrender or paid up values", "mis-selling", "lapsing", "miscellaneous".[46] The offices of OLTI had noted, as part of its analysis of complaints data, that its highest number of complaints were in relation to claims declined and those in relation to poor service.[47] 2018 was the year in which OLTI had begun its reporting journey to incorporate the TCF outcomes as categories of complaints received by the office.[48]

5.3. The alignment of complaints reporting within the financial services industry, specific to insurance

The ombud schemes have historically reported on their complaints statistics publicly through their annual reports. The FSCA has recognised the need to improve on these reporting capabilities and create standardisation across the entire sector. The Regulator initiated this process with the conduct of business return, wherein insurers were required to submit data relating to their complaints, including policy and claims data.[49] The guidelines were intended to provide the industry with guidelines for interpretation, reflecting how the Regulator would interpret the terminology.[50] The purpose of same was to ensure that the manner in which the Regulator interpreted same was the manner in which the industry interpreted same.[51] The CBRs were to be incorporated into the supervision of market conduct, which formed part of the off-site framework.[52] The granular detail reflecting the categories of reporting are for purposes of the Regulator understanding whether there are market conduct concerns arising.[53] Whilst the data is specifically designed to provide an understanding of the nature and complexity of a financial institution's business, same provides great insight into trends in terms of data and root

[44] OLTI *Annual Report 2018* 12.
[45] *Ibid.*
[46] *Idem* at 14.
[47] *Ibid.*
[48] *Ibid.*
[49] FSB *CBR Guideline* 1.
[50] *Ibid.*
[51] *Ibid.*
[52] FSB *CBR's Revised Categorisation* 1.
[53] *Idem* at 2.

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cause analyses arising out of the complaints received for the financial institution.[54] Each area of data ties back to a TCF category which is an indicator of where the issue could potentially exist. A brief explanation of the information is set out below:

Business composition: this is specific to trends relating to sales such as lapses or policies not taken up by a customer.[55] It would also relate to cancellations, depending on how the sales are made.[56] Depending on the information which is received, the Regulator would understand whether there are elements of mis-selling leading to unfair customer outcomes.[57]

Distribution and binder costs: these statistics provide information regarding the financial institutions capability and the reliance it places on external parties.[58] It is important to track information relating to same from a complaints perspective in that there is an expectation that a third party with whom a financial institution contracts bears the same onus of market conduct compliance as would a financial institution.[59] The difference lies in the manner in which the Regulator holds an institution accountable.[60] Based on the TCF guidelines, the insurer remains the accountable institution.[61] Therefore the insurer must ensure that any party with whom it contracts treats its customers in accordance with fair market outcomes and aligns to the principles of TCF.[62]

Claims management: these statistics relate to the numbers and value of claims received, paid, repudiated as well as outstanding claims.[63] The purpose of this section is to understand whether a financial institution has a fair and efficient process for purposes of handling claims.[64] Complaints relating to claims service are an indicator of a market conduct concern as it may indicate that a financial institution take a a lengthy period to finalise a claim, resulting in unfair conduct.[65] The longer a claim remains outstanding, the longer a customer is left without an outcome relating to the claim.

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[54] *Ibid.*
[55] *Ibid.*
[56] *Ibid.*
[57] *Ibid.*
[58] *Ibid.*
[59] FSB *TCF complaints management* 13.
[60] *Ibid.*
[61] *Ibid.*
[62] *Ibid.*
[63] FSB *CBR's Revised Categorisation* 2.
[64] *Ibid.*
[65] FSB *TCF complaints management* 13.

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Complaints management: its purpose is to assist identify trends, root causes for complaints and to be in a position to establish areas of improvement relating to product offerings or services offered to customers.[66]

Add-on/Rider benefits: this is included in the CBR reporting to gain a better understanding of additional benefits offered to clients by financial institutions. It is beneficial to understand which products or services add-ons supplement.[67]

CBR reporting was initially done as a "best effort" in order to get financial institutions ready for the formal submission requirements.[68] However, based on submissions received, the FSCA was already in a position to detect concerns relating to the information which was provided. Clarity was required in order for a clear understanding of the data.[69] Such instances included the manner in which repudiations were reported – the FSCA was of the view that the information was inaccurate and that insurers were to review definitions and report on same in accordance with set criteria.[70] Other instances included areas where "other" was selected as an option. Due to the wide interpretation, detailed reasons were required from the financial institution when selecting "other" in order for the FSCA to gain an understanding of the data.[71]

With regard to the CBR submissions, the financial institutions have been provided with guidelines and strict timelines for reporting. These are submitted on a quarterly basis, whereafter the FSCA engages via onsite discussions in order to obtain clarity around data submissions.[72] Based on the FSCA's analysis of the data, there are ongoing changes to the submission requirements to incorporate more detailed feedback.[73] Progress has been made since the inception of the CBRs as the submissions are now considered to be made on true and correct information as opposed to initially being scored as "best effort" reporting. These efforts in terms of reporting in conjunction with the existing and enhanced reporting capability of the various ombudsman schemes will support the FSCA to achieve its strategy relating to market conduct. The FSCA must continue to engage with the industry and various forums to learn and

[66] FSB *CBR's Revised Categorisation* 2.
[67] *Ibid.*
[68] FSCA *Communication 1 of 2019* 1.
[69] *Idem* at 3.
[70] *Ibid.*
[71] *Ibid.*
[72] *Idem* at 4.
[73] FSB *CBRs Guidance note 15 December 2017* 2.

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continuously improve to attain best practice-levels where data analyses and reporting are concerned.

5.4. Final remarks and conclusion

South Africa has been through many substantive and regulatory reforms from a regulatory perspective, with the latest piece of legislation being the Consumer Protection Act 68 of 2008, which sets a high standard for protecting customers, and the FSRA, discussed earlier.[74] The different sets of legislation protect customers to varying degrees. However, the financial services industry sets itself apart from other industries in that it requires specific designs based on the risks, impact and "strangeness" of its offerings.[75] Regulation of the financial services industry becomes difficult due to the gaps created between the various pieces of legislation, in effect customer protection legislation and financial services legislation.[76]

With this background, it becomes clear that the financial services industry is to be held to a higher standard when compared to other industries. Is this fair, considering that there are variations between the services offered or products being sold? There is risk to the customer, however, the customer, in an ideal scenario would be made aware of the risk prior to undertaking same. If there was a failure in terms of awareness, there ought to be a penalty against the financial institution for this failure. The current status quo appears to illustrate that the failure is established when the damage has already occurred and the customer has been prejudiced, thereby imposing financial hardship on a customer.[77]

As discussed, there are primarily two types of insurance which is available to customers, that of long-term insurance and short-term insurance. The volume of complaints received and published by the ombudsman schemes is an illustration of the market conduct concerns and trends relating to the weakness of the controls.[78] Hence, the need to strengthen the oversight of market conduct within the financial services industry,[79] Within the long-term sector, the complaint trends illustrate that the penalties relating to early termination of retirement and other

[74] Treasury *A safer financial sector to serve South Africa better* 41.
[75] *Ibid.*
[76] *Ibid.*
[77] Treasury *A safer financial sector to serve South Africa better* 41.
[78] *Idem* at 44.
[79] *Ibid.*

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savings policies are extremely high. Based on an analysis of these complaints, regulations were passed to reduce these charges and limit the commission that would generally be paid upfront.[80]

On short-term, one of the greatest challenges from a market conduct perspective was particularly on credit insurance. The objective would be to protect customers who borrow and their dependents from their asset being repossessed in the event of a death or loss of income. Are the objectives being met? If they are, why would be there be a trend of complaints relating to these types of cover? Considering the landscape within the South African economy and the unemployment rate, this type of cover would be required. However, the market conduct trends which arise out of the complaints data received by the Regulator have raised concerns, which concerns will be reviewed to ensure that the objectives of the product are met and that there are no concerns from a customer point of view.[81] It is the writer's view that the concerns which are identified provide the view that the customer is placed at a disadvantage due to the limited knowledge which it has in relation to the financial institution. Is the fear of the "big corporate" versus the "poor customer" mindset a reality? Does the Regulator have a valid concern in relation to the market conduct concerns that have been raised?

In the writer's view, there is "truth" to the concerns which have been raised. The various publications on complaints data as well as the enforcement actions taken are a clear indication that these are valid. However, the unfairness from a financial institution perspective is that there are financial institutions who incorporate and build market conduct practices into their daily operations where the customer is "at the heart" of the business. However, due to the behaviour of certain institutions, unfortunately, the rest of the financial institutions have to compensate accordingly.

This chapter dealt with reporting on complaints management as well as its intention. What is interesting to note is that the intention sought by the Regulator becomes apparent, however, same does not arise without challenges which face the financial services industry. The components which were addressed in this chapter were specific to the landscape as it had changed, what its intention was and what the potential for the change would unfold. The next chapter deals with complaints management within other jurisdictions and is intended to share the experiences therein.

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[80] *Ibid.*
[81] *Ibid.*

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Chapter 6: Evaluation of the South African framework against foreign jurisdictions and international best practices

6.1. Introduction

This chapter deals with complaints management within the jurisdictions of the United Kingdom and Australia. These countries have adopted the Twin Peaks approach within their regulatory environments and have adopted and evolved same through experience and learnings on their respective journeys. South Africa, being new to this landscape could reflect on their adoption techniques to understand how best to implement such an approach within its context

6.2. Background

Regulatory structures differ and are positioned with their own sets of strengths and weaknesses.[1] It is difficult to establish best practice and the ideal structure as each country and system has its own sets of challenges.[2]

The historic issue within the financial services industry in South Africa has been to establish a consistent manner to track how financial services providers treat their customers.[3] The expectation has always been for financial services providers to treat their customers in a fair manner.[4] Market conduct is an essential requirement in terms of regulation in that financial institutions generally have greater power over their customers due to the wealth of knowledge and experience which exists.[5] Historically, financial institutions have shown an ability to exploit this power over their customers.[6] Complaints information has provided context and insight into this abuse.[7] It was on this basis that there was a need to strengthen the regulation which governs market conduct.[8] Market conduct regulation provides a twofold benefit in that it restricts the abuse and complements prudential regulation.[9]

Regulators have struggled to establish how to incorporate the principles of treating customers fairly into the daily operations of financial institutions.[10] Within the UK environment, the FCA

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[1] Treasury *A safer financial sector to serve South Africa better* 29.
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] *Ibid.*
[6] *Ibid.*
[7] *Ibid.*
[8] *Ibid.*
[9] *Ibid.*
[10] Feasibility *A report prepared for the FSB, TCF complaints management* 2.

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had set out a set of principles and rules.[11] The TCF principle was expressed as a principle-based approach.[12] It became clear that a hybrid approach was required in that the rules should be detailed and the principles broad to allow for adequate implementation with clear guidance.[13] Whilst it is understood that rules and principles should be in place, there are other factors which must be considered in order for the approach to be successful.[14] Financial institutions must buy into the concept and not consider same a compliance requirement. There should be an incentive for performing according to the requirements.[15] A failure to do so should result in a consequence.[16] The rules and principles collaboratively set out these requirements.

The challenge is that, when a consequence is imposed, the wrong has already occurred and the customer is in distress.[17] At the stage of complaining, the customer had already been subjected to a degree of unfair treatment and was perhaps at a stage where not much could be rectified.[18]

The new framework in South Africa, through the implementation of TCF, requires firms to incorporate fair treatment throughout the product lifecycle.[19] It forces the financial institution to consider and cater for the customer during the design phase of the product, the marketing phase, advice as well as point of sale phases.[20] There is an underlying criterion for a re-evaluation of a financial institution's culture specific to customer and its fair treatment thereof.[21]

Examples of a positive incentive would be the ability to perform well, and which performance is shared within the public domain. An example of this would be statistics relating to performance in relation to complaints. Within the South African context this would refer to the ombudsman statistics that are published on an annual basis. The FSCA has plans to publish statistics relating to claims and complaints in future. The consequence of a failure to adhere to the requirements result in regulatory breaches with enforcement action, which enforcement

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[11] *Ibid*.
[12] *Ibid*.
[13] *Ibid*.
[14] *Ibid*.
[15] *Ibid*.
[16] Treasury *Draft Market Conduct Paper* 91.
[17] *Ibid*.
[18] Treasury *A safer financial sector to serve South Africa better* 42.
[19] FSB *TCF complaints management* 9.
[20] FSB *TCF complaints management* 9.
[21] Treasury *A safer financial sector to serve South Africa better* 42.

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action is published. In South Africa, the FSCA has confirmed that this is the mandate which they have been provided with and which they will act upon when required to do so.[22]

In the UK, the approach adopted is reactive and pre-emptive from a supervisory perspective.[23] This implies that the FCA has a model wherein they diagnose, monitor for the diagnosis, prevent to mitigate the risk and effect remedial action where necessary.[24] Whilst it is acknowledged that some risk will occur – where there is prejudice to a financial services customer – the extent of prejudice is limited.[25] Australia has adopted the same approach and is in a position to adjust its strategy based on key indicators which it identifies in its initial stages of diagnosis.[26] These strategies and approaches make it clear that supervision should also be risk-based in that Regulators should be spending a greater degree of time and effort on the areas of highest risk.[27]

The World Bank developed a set of regulatory requirements specific to the insurance sector.[28] Some of these requirements have been incorporated into existing legislation and subordinate legislation within the South African context – for example, the Code of Conduct in the FAIS Act incorporates some of these principles. Some of these extend to the nature and manner of providing advice to financial customers. It further confirms what is allowed and what will not be tolerated. It sets out the manner in which advice should be rendered and what the minimum requirements for disclosure to customers are.[29]

The TCF categorization of complaints incorporates complaints relating to advice as well as the information which is provided to customers.[30] Complaints relating to information provided would provide trends relating to the requirement in the regulations and whether same was complied with.[31] These trends would include whether the information provided was clear, understandable, complete, misleading and whether the extent to which the customer was dissatisfied.[32] The feedback arising out of complaints will incorporate whether information was

[22] FSCA *Regulatory Strategy* 57.
[23] Treasury *Draft Market Conduct Paper* 91.
[24] *Ibid*.
[25] *Ibid*.
[26] *Ibid*.
[27] *Ibid*.
[28] World Bank *Good practices for consumer protection* 69.
[29] Section 3(1) of the *General Code of Conduct for Authorised Financial Services Providers and their Representatives*.
[30] FSB *TCF complaints management* 11.
[31] *Idem* at 12.
[32] *Ibid*.

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provided at all stages and not only at the point of sale.[33] It is anticipated to include the specific product and the medium in which the information was provided.[34] The expected outcome is to establish compliance with the rules and to understand whether a financial institution takes into consideration the specific need of the market it is targeting and whether the information provided is suitable.[35] This illustrates that the South African context attempts to align with international standards and has a benchmark for best practice principles.

6.3. The regulatory framework of the United Kingdom (UK)

The UK passed the Financial Services Act of 2012, in respect of which section 6 changed the Financial Services Authority into the Financial Conduct Authority (FCA) and which Act generally brought the new regulatory structure into force. The UK launched the Twin Peaks model in April 2013 when section 6 of the Financial Services Act of 2012 amended the Financial Services and Markets Act of 2000 (FSMA).[36] The regulatory bodies of the FCA and Prudential Regulation Authority (PRA) were established in sections 1A and 2A of the FSMA.[37] The structure in chapter 1 of the FSMA set out powers and functions for the Financial Conduct Authority (FCA), which regulator was responsible for conduct of business and market issues for all firms.[38] Its core function is to take action before customers are prejudiced. In this regard, it needed to conduct thematic reviews and an analysis on potential concerns.[39] This would support it in its strategy to review a product life cycle from the onset to its distribution with the ability to prevent products from being marketed where it illustrated an intention to result in poor customer outcomes.[40]

Whilst the overarching objective of the FCA is to ensure that the markets perform well, it has three operational objectives, which include: ensuring a high degree of protection for financial customers; ensuring the integrity of the financial system within the UK and promoting effective competition to ensure the best interests of customers within the financial services market.[41]

[33] *Ibid*.
[34] *Ibid*.
[35] *Ibid*.
[36] See also FSB *TCF complaints management* 2.
[37] See also Chartered Insurance Institute *Toward Twin Peaks* 1.
[38] S 1B of the FSMA. See also Chartered Insurance Institute *Toward Twin Peaks* 1.
[39] Chartered Insurance Institute *Toward Twin Peaks* 1.
[40] *Ibid*.
[41] S 1B read with the provisions of ss 1C to 1 E. See also Chartered Insurance Institute *Toward Twin Peaks 1*.

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The PRA on the other hand, would have Its focus on ensuring financial stability. It would be based within the Bank of England and its intention would be to "ensure that firms can fail without bringing down the entire financial system".[42]

Prior to this change in 2012, the UK government had been urged to revisit the Financial Services and Markets Act of 2000 (FSMA) to ensure a coherent piece of legislation for reform. The FSMA sets out the "consumer protection objective" of the FCA, specifically in respect of "securing an appropriate degree of protection for consumers".[43] In order to reach its objectives, the FCA is authorised to provide guidance to the industry.[44] For purposes of this dissertation, the functions of the FCA under chapter 1 of the FSMA as set out in section 1B(6) are noteworthy:

> "For the purposes of this Chapter, the FCA's general functions are —
>
> (a) its function of making rules under this Act (considered as a whole),
>
> (aa) its function of making technical standards in accordance with Chapter 2A of Part 9A;
>
> (b) its function of preparing and issuing codes under this Act (considered as a whole),
>
> (c) its functions in relation to the giving of general guidance under this Act (considered as a whole), and
>
> (d) its function of determining the general policy and principles by reference to which it performs particular functions under this Act."

The FCA has a proactive manner of intervening at the onset of a product lifecycle to prevent unfair customer outcomes.[45] Similar to South Africa, the process was initiated prior to the implementation of Twin Peaks in that the Regulator had become involved in the review of

[42] Chartered Insurance Institute *Toward Twin Peaks* 1. See s 2B of the FSMA.
[43] Section 1C(1) of the FSMA.
[44] Section 139A of the FSMA. See also section 1B(5) of the FSMA and the FCA Business plan 2017/18 13 in respect of adherence to regulatory principles when it comes to discharging obligations.
[45] FCA, Business plan 2017/18 at 3.

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retail product development of specific products much earlier.[46] The intention of the FCA is further to be in a position to review and respond to complaints from customer groups.[47]

The system aims to create a level playing field, allowing customers to be in a position to compare and choose products that are appropriate to their specific needs.[48] It caters for customers to be in a position to compare products from financial institutions which products would be of the same offering.[49] The general approach is customer-based, in that financial institutions should place the best interest of the customer at the foundation of their decisions.[50] The TCF initiative is expected to form the basis of this. The intention is for issues to be identified upfront and the actions being preventative as opposed to reactive.[51]

The FCA has mechanisms in place to support it and to understand whether financial institutions are in a position to identify, manage and reduce unfair outcomes to its customers.[52] Whilst the FCA's aim is to eliminate risks upfront, it is not ignorant to the fact that there will be risks which are realized post-sale of a financial services product.[53] Its strategy is therefore extended to include post-sale barriers and transaction handling, in that it must be in a position to assess how a financial institution treats its customer after the sale.[54] The FCA leverages off its ability to interact with customers and its supervisory base in terms of complaints analysis to establish how financial services customers are being treated by financial institutions.[55] The approach

[46] *Idem* at 4. Although reference is henceforth made to the FCA's planning in this regard, the Regulator's approach in respect of consumers is firstly underscored by its mandate set out in section 1C of the FSMA: "(1) The consumer protection objective is: securing an appropriate degree of protection for consumers. (2) In considering what degree of protection for consumers may be appropriate, the FCA must have regard to - (a) the differing degrees of risk involved in different kinds of investment or other transaction; (b) the differing degrees of experience and expertise that different consumers may have; (c) the needs that consumers may have for the timely provision of information and advice that is accurate and fit for purpose; (d) the general principle that consumers should take responsibility for their decisions; (e) the general principle that those providing regulated financial services should be expected to provide consumers with a level of care that is appropriate having regard to the degree of risk involved in relation to the investment or other transaction and the capabilities of the consumers in question; (f) the differing expectations that consumers may have in relation to different kinds of investment or other transaction; … (h) any information which the scheme operator of the ombudsman scheme has provided to the FCA pursuant to section 232A." The approach is secondly informed by the regulatory principles set out in section 3B(1) of the FSMA (as per section 1B(5)(a)).
[47] FCA, Business plan 2017/18 at 4.
[48] *Ibid.*
[49] *Ibid.*
[50] *Ibid.*
[51] *Ibid.*
[52] *Ibid.*
[53] *Ibid.*

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requires flexibility in that the FCA may be required to provide greater focus and oversight on certain financial institutions as opposed to others.[56]

This is essentially based on three principles: supervision of financial institutions; engagement and action arising out of supervision; and reviews.[57] The FCA adopts this approach by categorizing financial institutions based on their side and customer base. This allows segmentation of the financial services industry to establish which financial institutions require greater oversight, meaning that financial institutions who have a large customer base consisting of retail customers versus smaller financial institutions are treated somewhat differently.[58] Whilst the intention is to have lower levels of supervision on smaller financial institutions, the extent of oversight will depend on the smaller financial institutions' ability to demonstrate practices of good customer outcomes to the FCA.[59] A failure to evidence this will result in the same degree of supervision and oversight as that of the larger financial institution, resulting in a more intrusive approach from the FCA.[60] The strategy of the FCA is earlier intervention and this extends to include, amongst others, the following:

- **Publication of enforcement action:** The FCA has been utilizing its power in this regard to make examples of financial institutions who do not adhere to the principles allowing for, and incorporating, the fair treatment of customers.[61] The FCA utilises the power to publish enforcement actions which will set out the details of the financial institution as well as a summary of actions taken. This is intended to "name and shame" financial institutions who do not adhere to the fair practice principles. In South Africa, the Regulator must engage with the relevant financial institution in order to gain insight and context into the work being done to rectify any untoward conduct. Financial institutions are expected to report any concerns to the Regulator and ensure that these concerns receive the required attention to rectify the identified issue.
- **Market intelligence gathering and research**: this is intended to include research as well as the current trends within the market to provide customers with a better view of the types of risks that they need to be aware of as well as where they exist.[62]

[57] *Idem* at 5. See also section 1L of the FSMA which sets the foundation for the FCA's authority to supervise, monitor and enforce.

See section 205 of the FSMA.

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- **Thematic reviews and supervisory visit**s: the FCA envisage that this approach will support financial institutions in providing evidence illustrating their approach to placing customers at the heart of what they do.[63]
- **Engagement with customer**s: the FCA seeks to build rapport and a better relationship with customers in order to gain an understanding of customer behaviour.[64] The relationship building is anticipated to take place through various forums, which would include social media, road shows, focus groups, face to face interactions, etc.[65] The FCA analyses customer information provided through complaint information, ombudsman schemes and any external or public research.[66]

The FCA issues guidance under the FSMA which sets out what firms should do to comply with their obligations under the respective principles to ensure the fair treatment of its customers.[67] The FCA handbook contains a complete record of the legal instruments within the UK and presents any changes made in a single consolidated format. The powers afforded to the FCA under the FSMA are set out in the handbook. The FMSA makes it mandatory for the FCA to make rules and provide guidance and codes.[68] The handbook provides financial institutions with the business standards, regulatory process and any redress which is specific to market conduct. There are various other processes and standards, however, same is not discussed in this dissertation as it falls wide of the scope of market conduct.

6.4. The regulatory framework of Australia

In Australia, the Twin Peaks model consists of two regulators, being the Australian Prudential Regulation Authority (APRA) and Australian Securities and Investments Commission (ASIC).[69] The APRA is responsible for prudential regulation and ASIC is responsible for consumer protection and market conduct.[70] It was anticipated that the blurred lines regarding

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[66] *Ibid.*
[67] FCA, FG21/1, 3
[68] Section 138G of the FSMA.
[69] Schmulow (2017) "Twin Peaks: An analysis of the Australian Architecture" Paper presented at the 2016 Global Forum for Financial Consumers, SKK University, South Korea, November 4-5, 6. In additional to section 2 of the Australian Securities and Investments Act 51 of 2001 (ASIC Act) (read with *Gazette* 2001, No. S285 as per endnote 3 on "Federal Register of Legislation", see also the Australian Prudential Regulation Authority Act 50 of 1998.
[70] See *inter alia* section 1(2) of the ASIC Act and section 8 of the APRA Act. Schmulow (2017) "Twin Peaks: An analysis of the Australian Architecture" Paper presented at the 2016 Global Forum for Financial Consumers, SKK University, South Korea, November 4-5, 6.

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regulatory responsibilities would become clear and that each Regulator would have its own set of responsibilities for which it would be held accountable.[71]

ASIC administers and enforces a range of legislation, some of which are not specific to market conduct regulation e.g. ASIC is responsible for overseeing the registration and regulation of companies in Australia in terms of section 5B of the Corporations Act 50 of 2001 . However, ASIC is Australia's integrated corporate, markets, financial services and consumer credit regulator and thus, from a Twin Peaks perspective, the financial sector market conduct/consumer protection regulator.[72]. It has been set up under the Australian Securities and Investments Commission Act of 2001 and carries out most of its work under the Corporations Act. Its role under the ASIC Act is to:

> "Maintain, facilitate and improve the performance of the financial system and entities in it … Promote confident and informed participation by investors and consumers in the financial system … Administer the law effectively and with minimal procedural requirements … Receive, process and store, efficiently and quickly, information we receive … Make information about companies and other bodies available to the public as soon as practicable … Take whatever action we can, and which is necessary, to enforce and give effect to the law."[73]

The approach of Twin Peaks, specific to the functions of ASIC, is to protect financial customers, specifically retail customers from unfair practices which inevitably results in systemic risk.[74] This has been the long-standing debate on whether there is equality between consumer protection and financial stability. A consequence of a failure by the prudential regulator will inevitably take precedence over market conduct outcomes.[75] A financial failure is more serious than poor treatment of customers – or is it?

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[71] Schmulow (2017) "Twin Peaks: An analysis of the Australian Architecture" Paper presented at the 2016 Global Forum for Financial Consumers, SKK University, South Korea, November 4-5,13.
[72] See Part 2 of the ASIC Act.
[73] ASIC 'What we do' www.asic.gov.au. This breakdown has clearly been derived from *inter alia* section 12A of the ASIC Act, which determines the following in subsections (2) and (3): "ASIC has the function of monitoring and promoting market integrity and consumer protection in relation to the Australian financial system…. ASIC has the function of monitoring and promoting market integrity and consumer protection in relation to the payments system by: (a) promoting the adoption of approved industry standards and codes of practice; and (b) promoting the protection of consumer interests; and (c) promoting community awareness of payments system issues; and (d) promoting sound customer-banker relationships, including through: (i) monitoring the operation of industry standards and codes of practice; and (ii) monitoring compliance with such standards and codes."
[74] *Ibid.*
[75] *Idem* at 15.

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The theoretical intention with Twin Peaks is to reach a stage where there is a balance between financial stability and the achievement of fair market outcomes. Twin peaks is aimed at safeguarding and protecting customers as much as is possible while still ensuring the financial soundness of financial institutions.[76] The strategy of the ASIC is to detect, understand and respond.[77] The ASIC adopts a risk-based approach to understanding areas of risk. The approach detects inappropriate behaviour through surveillance, breach reports, reports from the public and whistleblowers, and data accumulation and analysis.[78] The information is utilized to adopt a proactive approach allowing ASIC to respond as quickly and efficiently as possible.[79] The response aspect extends to include disruption of harmful behaviour, enforcement action, communication in terms of the actions taken, education of customers and investors, and providing guidance and advice.[80]

ASIC has key focus areas, including taking action against financial institutions who prey on the poor retail customer; disrupting the mis-selling of harmful products and the provision of poor advice to customers; acting against scams; assisting financial institutions to ensure that proper support and assistance is provided to customers, insurance claims are processed efficiently and with utmost good faith; engaging proactively with financial institutions to ensure fair business standards; providing customers with information to manage their finances; and taking action to ensure that financial institutions provide accurate information to customers.[81] ASIC's strategic planning framework supports the strategy for each year. Trends from prior periods are identified within the financial services environment.[82] Predictive analytics in the form of a threats, harms and behaviour-framework is applied to understand the real threats to customers.[83] The ASIC then decides on key focus areas for the upcoming year, which focus areas drive the priorities for the period.[84] This could serve as a recommendation within the South African context.

The effectiveness of the Twin Peaks model is dependent on its agility and the respective government's commitment to flexibility.[85] The model requires continuous improvement and

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[76] *Idem* at 21.
[77] ASIC *Strategic outlook* 3.
[78] *Ibid.*
[79] *Ibid.*
[80] *Ibid.*
[81] ASIC *Corporate plan 2020-24, Focus 2020-21* 9.
[82] *Ibid.*
[83] *Ibid.*
[84] *Ibid.*
[85] Moodley *The Twin Peaks model: a critical analysis of its effectiveness in SA* 56.

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the ability to make decisions quickly and efficiently.[86] The adjustments are to be made as the economy develops.[87] Australia demonstrated this in its strategy change with the onset of the COVID-19 pandemic.[88] The ASIC was in a position to adjust its strategy to create a renewed focus whilst keeping with its underlying core principles.[89]

ASIC had undertaken a review of conduct risk within financial institutions to obtain a market view of how this was being done.[90] The review had revealed feedback in a positive and negative context in that there were good and poor practices.[91] The approach was to establish how the financial institutions managed their conduct risk.[92] Other than looking at the culture of the financial institution, ASIC extended its scope to include how the financial institutions proactively identified conduct risk; whether it encouraged all staff members to report on and be accountable for conduct within the financial institution; whether the financial institution supported staff in areas which required improvement and the financial institution had oversight of conduct risk.[93] ASIC confirmed that good practice warranted the involvement of senior management as well as the Board of the financial institution.[94]

The general insurance code of practice sets a benchmark for self-regulation in the financial services sector. The Code was developed by the industry in consultation with multiple stakeholders.[95] The Code was introduced in 1994 by the Insurance Council of Australia as a voluntary code. It is regularly reviewed and updated. Whilst ASIC is a stakeholder who is consulted with for the Code, it is independently monitored and enforced by the Code Governance Committee.[96] The Code shapes the manner in which the insurance industry behaves, treats people and approaches decision-making. The Code applies to all insurance companies who have adopted it. The Code is limiting in that it does not apply to all types of insurance, e.g. it does not cover workers compensation insurance, marine, motor vehicle injury, medical indemnity, reinsurance, life products issued by a life insurer and health insurance issued by a registered health insurer.

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[86] *Ibid.*
[87] *Ibid.*
[88] ASIC *Corporate plan 2020-24, Focus 2020-21* 9.
[89] *Ibid.*
[90] ASIC *Conduct Risk Management* 3 September 2020.
[91] *Ibid.*
[92] *Ibid.*
[93] *Ibid.*
[94] *Ibid.*
[95] ICA General Insurance Code of Practice 1.
[96] ICA General Insurance Code of Practice 3.

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6.5. The regulatory framework of South Africa: an analysis

There are certain aspects to consider in terms of the implementation of Twin Peaks in South Africa.[97] The pre-Twin Peaks silo approach resulted in inconsistent standards and requirements relating to the regulation of different industries, which inconsistency has resulted in regulatory arbitrage.[98] The Twin Peaks approach therefore sought to curb this risk, with two specific aims under two separate regulators: the PA would strengthen the financial safety and soundness of financial institutions; and the FSCA would protect financial customers and ensure that they receive fair treatment from financial institutions.[99] Twin Peaks was deemed to be the most appropriate model for the South African context. The following aspects were considered advantages for its implementation: Each regulator would have dedicated objectives with clear guidelines in terms of outcome; there would be less risk of one objective taking precedence over the other, such as financial stability overpowering market conduct risk; the approach would be more flexible to deal with arising complexities; and the risk of conflict would be lower.[100]

The Reserve Bank oversees financial stability on a macro-prudential level and the PA on a micro-prudential level. The prudential framework has been developed and evolved over a period. However, the market conduct framework had fallen behind. This is in line with the prior regime and illustrates the financial stability aim having priority over the market conduct risk in South Africa as well. Although it is envisaged that, with the implementation of Twin Peaks and the creation of the two separate regulators, that the market conduct framework will now receive the same, if not greater, degree of attention in order for its evolution, this is uncertain. The PA is intended to prevent frailness amongst the financial institutions. In essence, the model is intended to provide equal importance to the key functions, i.e. prudential regulation and market conduct or customer protection. There is a need for sharing of information, specifically at operational level between the two regulators. A failure to do so could result in a regulator not being in a position to respond in a timely manner. Within the South Africa context, does the Regulator have adequate insight into operational detail of financial institutions to be in a position to balance the position between financial stability and

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[97] Moodley *The Twin Peaks model: a critical analysis of its effectiveness in SA* 48.
[98] Treasury *Twin Peaks in SA: Response & Explanatory Document* 7.
[99] *Ibid.*
[100] Godwin (2017) "Australia's Trek toward Twin Peaks – comparisons with South Africa" *Law and Financial Markets Review* 151-153.

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market conduct. The writer's view is that the South African approach is still within its infancy stages, and it is likely that there will be an imbalance between the two regulators.

Financial institutions face a dilemma when it comes to the reporting function which is now split into reporting based on prudential requirements and conduct requirements.[101] The greatest impact would be in respect of financial institutions where an overlap exists.[102] Financial institutions would be required to split their own focus to ensure that the reporting and communication between the respective regulators meet expectations based on the respective regulators' objectives within the Twin Peaks regime.[103] Financial institutions would be required to train individuals to ensure that the skillset matches the new requirements. An example of a skillset would be those required in terms of market conduct risk. An in-depth understanding in order to identify, manage and address market conduct risk would be key to the function of individuals appointed to manage this task.[104] Systems and reporting capabilities would require development in order to ensure compliance with requirements as and when they become necessary.[105] The UK reforms are similar to the South African context, particularly in terms of the structures. There is a clear and distinct role for the central bank, a prudential regulator within the central bank, and a separate market conduct regulator.[106] Both countries place a priority on the independence of the regulators.[107] In this regard, the mechanisms put in place by the UK to manage compliance related issues are worth noting.

It is important to ensure that the objective of each regulator is defined. The boundaries must be clear. Supervision should be comprehensive, and it is necessary to have effective coordination between the Regulators. The collapse of the financial conglomerate in Australia demonstrated the need for operational sharing of information between the two regulators and the need for coordination between them.

6.6. Complaints management in the UK

The FCA's preferred approach would be to ensure that all financial services customers have a positive experience.[108] However, realistically, it appreciates that this will not always be the

[98] Moodley *The Twin Peaks model: a critical analysis of its effectiveness in SA.*
[102] *Ibid.*
[103] *Ibid.*
[104] *Ibid.*
[105] *Ibid.*
[106] FRRSC *Implementing a Twin Peaks model* 23.
[107] *Ibid.*
[108] FCA *Thematic Review Complaint Handling* 2.

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experience.[109] Therefore, it is important to be prepared for those instances where customers do have a need to complain.[110]

Complaints are a mechanism for financial institutions to understand the experience of their customers.[111] Complaints create an opportunity for financial institutions to learn from mistakes and enhance their products and services.[112] The FCA embarked on a review to understand how whether there were any barriers within complaints handling.[113] The intention of the review was to establish whether financial institutions did place customers at the center of their business.[114] In order for the FCA to understand whether there was evidence supporting fair market conduct outcomes, it needed to understand whether financial institutions had fair, effective and transparent processes in place when it came to complaints handling.[115] This would illustrate that financial institutions handled customer complaints in a reasonable, prompt and fair manner.[116]

The FCA sought to establish whether there were any barriers which inhibited a financial institution from placing its customer first.[117] The FCA's outlook on this was to determine if there were concerns within internal processes and how these could be enhanced to be included into the culture of treating customers fairly.[118] The thematic review highlighted that there are inconsistencies in definitions, and the manner in which financial institutions reported on and interpreted their data.[119] This resulted in ineffective root cause analyses and incorrect remedial action initiatives.[120] The FCA established that the financial institutions were committed to ensuring better customer outcomes and will be reviewing their complaints handling processes and practices to align to the expectations of the FCA.[121] An important aspect to highlight from the review, however was the fact that the reporting of complaints as part of management information was sometimes viewed as a compliance and tick box exercise.[122]

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[109] *Ibid.*
[110] *Ibid.*
[111] *Ibid.*
[112] *Ibid.*
[113] *Ibid.*
[114] *Ibid.*
[115] *Ibid.*
[116] *Ibid.*
[117] *Ibid.*
[118] *Idem* at 3.
[119] *Idem* at 24.
[120] *Ibid.*
[121] *Ibid.*
[122] *Ibid.*

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As part of the thematic review conducted in the UK, it was established that data reported during the complaints return was inconsistent.[123] The impact of inconsistent reporting could potentially result in inadequate analysis and feedback.[124] This would inhibit future remedial action, if any. The FCA established that the inconsistency was as a result of the definition of a complaint. The FCA handbook now defines a complaint as:[125]

> "Any oral or written expression of dissatisfaction, whether justified or not, from, or on behalf of, a person about the provision of, or failure to provide, a financial service or a redress determination, which alleges that the complainant has suffered (or may suffer) financial loss, material distress or material inconvenience and relates to an activity of that respondent, or of any other respondent with whom that respondent has some connection in marketing or providing financial services or products, which comes under the jurisdiction of the Financial Ombudsman Service."

Following the thematic review in 2013, the FCA sought to effect changes to the complaints handling practices within the financial services industry.[126] It sought to provide rules and guidance relating to how complaints should be responded to in a prompt and fair manner.[127] The FCA intended on implementing an alternative dispute resolution body, which extended to the ombudsman, of which subscription was on a voluntary basis.[128]

The existing complaint processes were lengthy and formal in nature.[129] Whilst one would acknowledge that some complaints required extensive feedback and engagement, there are others which can be resolved within a short period of time.[130] It would therefore be important to be in a position to segment complaints based on the type of complaint that is received.[131]

The FCA recognized that this segmentation would also allow for different skillsets to exist within the handling of complaints.[132] Depending on the nature and complexity of the complaint, staff members who had the relationship with the customer should be afforded the opportunity

[123] FCA *Thematic Review, Complaint Handling* 15.
[124] *Ibid.*
[125] FCA *Consultation Paper, improving complaints handling* 6.
[126] *Ibid.*
[127] *Ibid.*
[128] *Ibid.*
[129] *Idem* at 9.
[130] *Ibid.*
[131] *Ibid.*
[132] *Ibid.*

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to engage to resolve.[133] This would largely be driven by the customer's preference, meaning that, should the customer wish to deal with the individual who they know and trust, they ought to be at liberty to do so.[134]

The FCA realised that complaints data ought to be more granular, in effect the data should set out categories of complaints that are received.[135] It should extend to include the specific products to which they relate.[136] The data and reporting should extend to include the turnaround time of complaints – how quickly complaints are resolved and which categories of complaints these relate to.[137] The purpose of including more extensive data was to ensure consistency in same and to ensure correct data is reported upon.[138] The publishing of data could drive the FCA strategy on financial institution behaviour in that it can cause financial institutions to act to ensure that their data is of acceptable standard as this would increase their media profile.[139] It would further result in providing a better customer service.[140]

6.7. Complaints management in Australia

The Australian definition had been changed through a consultation process in 2020, because the Regulator had established that certain complaints were not being included in the complaints data.[141] The definition was updated and now forms part of the internal dispute resolution guide.[142] A complaint is therefore defined as

> "[An expression] of dissatisfaction made to or about an organization, related to its products, services, staff or the handling of a complaint, where a response or resolution is explicitly or implicitly expected or legally required."

A key area of focus was detecting issues, and this was done in the context of surveillance, breach reporting as well as data gathering.[143] Detection comprised of targeting the largest financial institutions to establish how they complied as well as identifying "red flags". The

[133] *Ibid.*
[134] *Ibid.*
[135] *Idem* at 15.
[136] *Ibid.*
[137] *Ibid.*
[138] *Idem* at 16.
[139] *Ibid.*
[140] *Ibid.*
[141] ASIC *Update to RG 165* 8.
[142] ASIC *Regulatory Guide RG271* 13.
[143] Schmulow (2017) "Twin Peaks: An analysis of the Australian Architecture" Paper presented at the 2016 Global Forum for Financial Consumers, SKK University, South Korea, November 4-5.

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Regulator analysed information they received to establish whether there was a need to act or monitor.[144]

6.8. Complaints management in South Africa: an analysis

The FSCA has supported the industry by engaging with financial institutions by means of ongoing supervision, routine on-site visits, thematic reviews and other formal and informal engagements.[145] The intention is to adopt a pre-emptive, proactive supervisory approach which will typically entail agreeing with institutions on remedial action to mitigate identified market conduct risks.[146] However, where the approach is not effective, the FSCA will take formal action.[147]

The FSCA strategy document confirms that complaints management and its monitoring will be a key supervisory approach.[148] It is clear that the regulator's intention is to utilize complaints data to gain insight into a financial institution's internal complaints processes and its effectiveness.[149] The expectation of the industry is that the data being collated and reported on is to ensure that same is analysed to gain an understanding of what their customers are saying through complaints.[150] Upon analysis, the financial institution would be expected to effect changes to enhance the customer experience where it has shown to be lacking.[151]

The South African context has undergone similar challenges as that within the UK environment in that there has been inconsistency in terms of the definition of a complaint and therefore inconsistency in process and reporting of same.[152] It was upon this basis that a complaint was defined as

> "an expression of dissatisfaction by a complainant, relating to a product or service provided or offered by a financial institution, or to an agreement with the financial institution in respect of its products or services and indicating that –

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[144] Godwin (2017) "Australia's Trek toward Twin Peaks – comparisons with South Africa", *Law and Financial Markets Review* 151 *et seq.*
[145] FSCA, *Regulatory Strategy*, 57
[146] FSCA, *Regulatory Strategy*, 57
[147] FSB *CBR's Revised Categorisation,* 2.
[148] *Ibid*
[149] Ernest & Young, FSR Act, implementing twin peaks and the impact on the industry
[150] FSCA, *Regulatory Strategy* 41.
[151] FSCA, *Regulatory Strategy* 41.
[152] FSB *TCF complaints management* 3.

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(a) the financial institution or its service provider has contravened or failed to comply with an agreement, a law, a rule, or a code of conduct which is binding on the financial institution or to which it subscribes;

(b) the financial institution or its service provider's maladministration or wilful or negligent action or failure to act, has caused the complainant harm, prejudice, distress or substantial inconvenience; or

(c) the financial institution or its service provider has treated the complainant unfairly and regardless of whether such an expression of dissatisfaction is submitted together with or in relation to a customer query."[153]

The above definitions highlight the need for consistency and standardization in terms of terminology as well as process to ensure that there is a streamlined and consistent approach which is evident amongst financial institutions and that the experience for the customer is the same. In my view, the definitions are fairly consistent across all countries.

An aspect which intrigues me is the specific reference to the financial institution included, and specifically referenced, in the definition. It implies that financial institutions have not been classifying or capturing complaints correctly and the definitions now clearly establish the obligation to do so.

Complaints data is important and financial institutions should encourage customers to lodge valid complaints, although it seems that financial institutions were not comfortable with revealing this information to the Regulators. In this regard, a more diplomatic and tactical approach may be required.

Complaints provide a view of where the issues are from a customer perspective, allowing financial institutions to work on improving the processes, products, and offerings to ensure that there are fair outcomes to customers. The Australian Securities and Investments Commission (ASIC) sets out clearly that customer complaints are a good source for the purpose of identifying systemic issues within a financial institution.[154] System issues have the potential to affect more than one customer and therefore financial institutions must be in a position to have the mechanisms in place to monitor, detect and address these types of issues.[155] Whilst the Regulators within these countries have identified the issues and concerns relating to the gaps

[153] *Ibid.*
[154] ASIC *Regulatory Guide RG271* 34.
[155] *Ibid.*

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in the definition of a complaint, it is questionable whether a mere change of definition is a practical solution to change the behaviour and culture that has been entrenched in this industry for decades.

Complaints handling and reporting has always been considered a compliance function from the perspective of the financial institution to show that it is in a position to demonstrate that it has a complaints management process, it meets the relevant minimum requirements in terms of reporting, and it is in a position to show that the complaint is resolved to the extent that it can demonstrate its stance by evidence supporting the outcome.

The question is whether these additional steps, consistent amongst the countries referred to above, have not merely increased the extent to which financial institutions are now expected to deal with complaints without truly changing the culture of the corporations involved.

6.9. Outcomes relating to data collection, analysis, and reporting

In the UK complaints reporting include the number of complaints registered, closed, and resolved in favour of the complainant, the amount paid in relation to resolution, the type of complaint consisting of the type of financial institution and product, and the reason for the complaint.[156]

Reporting of complaints within the Australian context include data at a minimum level in order to obtain an understanding of the volume and types of complaints being received.[157] This includes the number of complaints received, the number of complaints closed, the type of complaints, the turnaround time of acknowledgement and finalisation of complaints, complaint outcomes, the manner in which complaints were resolved, any issues identified, and the number of complaints escalated to the regulatory bodies.[158]

In South Africa, the minimum requirements relating to reporting on complaints management include relevant details of the complainant, reasons for the complaint, TCF categorisation of the complaint, turnaround times on complaints, volume of complaints received, finalised,

[156] FSB *TCF, complaints management* 7.
[157] *FCA, Consultation Paper, Improving complaints handling*
[158] *Idem* at 47.

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outstanding as well as the manner in which the complaints were resolved. It further should extend to include complaints which were escalated.[159]

The criteria for reporting appeared to be fairly consistent amongst all three countries. Its intended purpose was also consistent in that the regulators expected that financial institutions would utilise these reports and data to analyse the complaints for purposes of enhancing their business practices, processes, to implement training amongst staff, and to ensure better outcomes to financial services customers.[160] The regulators also had the intention of utilising the data for purposes of analysis and to establish the manner in which financial institutions ought to manage from a regulatory perspective. It is also standard practice amongst all three countries to have the complaints data published, however, the complaints data which is published is that of the ombudsman schemes, data relating to escalated complaints. The question to be posed in this regard is whether this is fair, considering the size, complexity, and model of the different financial institutions. Is the publication of the data understood and is it fair to provide the reporting in the format which alludes to the financial institutions being the same? Differences between financial institutions could be as simplistic as the direct model versus the broker-based model, which refers to direct being the financial institution have a direct relationship with the customer whereas as broker-based model would have an intermediary or broker who has the relationship with the customer. Is it therefore a fair practice to have all financial institutions as "one" when publishing the data in a public manner?

The UK, through its thematic reviews received such feedback and in February 2017 incorporated the size of a financial institutions' business into its public reporting.[161] I acknowledge the need to create a level platform relating to reporting on a comparative and like-for-like basis and submit there is much work to be done in South Africa in this regard.

6.10. Conclusion

The changes which were proposed, and which are being implemented within the South African context incorporate lessons from our international counterparts.[162]

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[159] *Ibid.*
[160] *ASIC, Strategic Outlook*
[161] FCA *Firm specific complaints data* 29 April 2021.
[162] *Idem* at 42.

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This chapter dealt with international markets and how South Africa is evolving to align to international standards, specific to complaints management. The components that were addressed were in relation to structure, process and reporting specifically. It was found that an entity is unable to adequately understand and detect concerns without adequate data and an analysis of same. Market conduct data, specific to complaints management is an evolving function, which aims to bring new, interesting and fruitful insights to both the financial institution as well as its customer. The next chapter deals with a summary and overview of complaints management within the insurance industry and what its expected outcomes ought to be.

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Chapter 7: Conclusion and recommendations

7.1. Introduction

The historic issue within the financial services industry has been to establish a consistent manner to track how financial services providers treat their customers.[1] The expectation has always been for financial services providers to treat their customers in a fair manner.[2] Market conduct is an essential requirement in terms of regulation in that financial institutions generally have greater power over their customers due to the wealth of knowledge and experience which exists.[3] Historically, financial institutions have shown an ability to exploit this power over their customers.[4] Complaints information has provided context and insight into this abuse.[5] It was on this basis that there was a need to strengthen the regulation which governs market conduct.[6]

Market conduct regulation provides a twofold benefit in that it restricts the abuse and complements prudential regulation.[7] The changes which were proposed and which are being implemented within the South African context incorporate lessons from our international counterparts.[8] The TCF approach for example does not place a sole reliance on financial institutions doing the right thing; the approach incorporates a more robust market conduct Regulator with a proactive and intrusive approach to supervision.[9] The intention is for all legislation to ideally work in a harmonized manner and to ensure that the relevant Regulators have the necessary toolkits and power to satisfy the overall strategy of market conduct.[10]

The financial services industry plays a vital role within the South African economy. It is therefore necessary to ensure that it is adequately regulated and supervised to promote transformation and financial inclusion.[11]The approach adopted requires a balance between rules based and principles-based regulation to ensure delivery of fair outcomes to financial services customers.[12] Strengthening of complaints management from a regulatory perspective was a key deliverable in terms of the changes which were committed to. This was not a

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[1] Treasury *A safer financial sector to serve South Africa better* 39.
[2] Treasury *A safer financial sector to serve South Africa better* 39.
[3] Treasury *A safer financial sector to serve South Africa better* 39.
[4] Treasury *A safer financial sector to serve South Africa better* 39.
[5] Treasury *A safer financial sector to serve South Africa better* 39.
[6] Treasury *A safer financial sector to serve South Africa better* 39.
[7] Treasury *A safer financial sector to serve South Africa better* 39.
[8] Treasury *A safer financial sector to serve South Africa better* 42.
[9] Treasury *A safer financial sector to serve South Africa better* 42.
[10] Treasury *Draft Market Conduct Paper* 36.
[11] FSCA *Regulatory Strategy* 31.
[12] FSCA *Regulatory Strategy* 38.

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standalone commitment in that the monitoring of same was a requirement to ensure enablement. Intrusive supervision and insight into how financial institutions deal with complaints and dispute resolution processes would be required in order to ensure adequate monitoring, tracking and implementation.[13] This would occur through the monitoring of complaints data provided by financial institutions as well as ombudsman schemes to allow the FSCA to identify and monitor market trends, governance and management failures as well as poor customer outcomes.[14]

An important aspect of understanding market conduct risk is to understand and establish its source. The components and make-up of the source assist to fix or resolve the identified risks.[15] The intention of market conduct regulation is to prevent, and in the event of prevention not being possible to manage the poor outcomes which arise from the manner in which financial institutions conduct their businesses, specifically where there is unfair treatment to customers and where the integrity of the financial markets and its integrity is undermined.[16] Overall, there has been great progress in terms of the structural regulatory reform.[17] The ongoing revision of the legal framework is intended to streamline the market conduct requirements for financial institutions.

7.2. Overview

In February 2011, South Africa committed to a safer financial sector.[18] Reforms relating to the financial sector were initiated and one of the core aspects was the commitment to improve the regulatory structures that support financial regulation.[19] The reforms were officially implemented, albeit in phases, from 2018 onwards. The FSRA empowers and increases the FSCA's ability to improve conditions, and provide protection, for customers where there is poor conduct or behavior from financial institutions; overcome adverse conditions; and enhance financial stability and financial sector integrity.[20] The legislation aims to ensure that

[13] FSCA *Regulatory Strategy* 41.
[14] FSCA *Regulatory Strategy* 41.
[15] FSCA *Regulatory Strategy* 41.
[16] Treasury *Explanatory policy paper accompanying COFI* 2.
[17] Treasury *Explanatory policy paper accompanying COFI* 3.
[18] FSB *TCF Road Map* 36.
[19] FRRSC *Implementing a twin peaks model* 2.
[20] FSB *Twin Peaks Newsletter* Issue 2.

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the FSCA is able to monitor and supervise the manner in which financial institutions conduct business to ensure the fair treatment of customers.[21]

TCF remains a core indicator of acceptable market conduct behaviour. It is embedded in financial sector regulation[22] as a regulatory and supervisory approach that seeks to ensure that financial institutions, including insurers, demonstrate and deliver clearly articulated fairness outcomes for financial services customers, such as insurance clients, throughout the typical financial product lifecycle.[23]

The TCF outcomes articulate the manner in which the FSCA expects financial institutions to deal with their customers.[24] The FSRA included the TCF approach in its framework by providing the FSCA with an explicit directive of promoting the fair treatment of financial customers and empowering it to make conduct standards that were aimed at ensuring that this directive was met.[25] COFI aims to further incorporate these principles, and its focus will be on retail customers.[26] Although COFI has a principles-based focus – meaning that it does not set out specific rules, but rather the intention of the rules[27] – it will still function alongside the FSCA's conduct standards that will be developed to ensure delivery of the six TCF outcomes.[28] The design of the COFI Bill will support the TCF outcomes-based approach.[29] The expectation is that the TCF aligned provisions of the Bill will be principles-based, while the more explicit conduct standards will be developed to underpin the delivery of the six TCF outcomes.[30] The TCF Roadmap contemplates that the delivery of TCF requires the development of a regulatory framework that ensures the balance between principles-based and rules-based regulation to ensure that financial institutions are able to deliver the desired outcomes of discipline and transparency in a consistent manner.[31]

The approach seeks to ensure fairness outcomes for customers delivered by an adequately regulated industry.[32] It further intends to incorporate customer confidence by ensuring the

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[21] *Ibid*.
[22] Millard and Maholo (2016) "Treating Customers Fairly: A New Name for Existing Principles" *THRHR* 594.
[23] FSCA *Regulatory Strategy* 37.
[24] FSB *CBR's Response to industry comments* 2.
[25] Sections 57 and 106 of the FSRA.
[26] Department Planning, Monitoring & Evaluation *Initial impact of COFI* 7.
[27] Treasury *Explanatory policy paper accompanying COFI* 11.
[28] *Ibid*.
[29] *Idem* at 50.
[30] *Ibid*.
[31] FSB *CBR's Revised Categorisation 2.*
[32] FSB *TCF complaints management* 20.

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supply of appropriate financial products and services through enhanced transparency and discipline.[33] TCF is to ensure that financial institutions consider the fair treatment of customers throughout the product lifecycle.[34] Financial institutions would be expected to demonstrate this through monitoring and management behaviours.[35] TCF's fairness outcomes apply to all the stages of a typical product life cycle.

An important aspect of understanding market conduct risk is to understand and establish its source. The components and make-up of the source assist to fix or resolve the identified risks.[36] The intention of market conduct regulation is to prevent, and in the event of prevention not being possible to manage the poor outcomes which arise from the manner in which financial institutions conduct their businesses, specifically where there is unfair treatment to customers and where the integrity of the financial markets and its integrity is undermined.[37] Overall, there has been great progress in terms of the structural regulatory reform.[38] The ongoing revision of the legal framework is intended to streamline the market conduct requirements.

The TCF approach for example does not place a sole reliance on financial institutions doing the right thing; the approach incorporates a more robust market conduct Regulator with a proactive and intrusive approach to supervision.[39] The intention is for all legislation to ideally work in a harmonized manner and to ensure that the relevant Regulators have the necessary toolkits and power to satisfy the overall strategy of market conduct.[40] The financial services industry plays a vital role within the South African economy. It is therefore necessary to ensure that it is adequately regulated and supervised to promote transformation and financial inclusion.[41] The approach adopted requires a balance between rules based and principles-based regulation to ensure delivery of fair outcomes to financial services customers.[42]

Strengthening of complaints management from a regulatory perspective was a key deliverable in terms of the regulatory changes which were committed to. This was not a standalone commitment in that the monitoring of same was a requirement to ensure compliance. Intrusive

[33] *Ibid*.
[34] *Ibid*.
[35] FSB *TCF Road Map* 8.
[36] *Ibid*.
[37] Treasury *Explanatory policy paper accompanying COFI* 2.
[38] *Idem* at 3.
[39] *Ibid*.
[40] Treasury *Draft Market Conduct Paper* 36.
[41] FSCA *Regulatory Strategy* 31.
[42] *Idem* at 38.

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supervision and insight into how financial institutions deal with complaints and dispute resolution processes would be required in order to ensure adequate monitoring, tracking and implementation.[43] This would occur through the monitoring of complaints data provided by financial institutions as well as ombudsman schemes to allow the FSCA to identify and monitor market trends, governance and management failures as well as poor customer outcomes.[44]

The FSCA has supported the industry by engaging with financial institutions by means of ongoing supervision, routine on-site visits, thematic reviews and other formal and informal engagements.[45] The intention is to adopt a pre-emptive, proactive supervisory approach which will typically entail agreeing with institutions on remedial action to mitigate identified market conduct risks.[46] However, where the approach is not effective, the FSCA will take formal action.[47]

The FSCA strategy document confirms that complaints management and its monitoring will be a key supervisory approach.[48] It is clear that the regulator's intention is to utilize complaints data to gain insight into a financial institution's internal complaints processes and its effectiveness.[49] The expectation of the industry is that the data being collated and reported on is to ensure that same is analysed to gain an understanding of what their customers are saying through complaints.[50] Upon analysis, the financial institution would be expected to effect changes to enhance the customer experience where it has shown to be lacking.[51]

The intention of the shifts in the regulatory environment specific to complaints management is to support the delivery of fair outcomes to customers within the financial services sector.[52] It is to ensure that monitoring becomes an enabler to establish that the outcomes are being achieved and to ensure that, if a risk of poor outcomes exists, there are steps to detect and mitigate such risk. The approach differs from the historic approach wherein random supervisory visits were done to determine compliance with the regulations and where addressing poor outcomes was a slow process, if initiated.[53] The supervisory approach has

[43] *Idem* at 41.
[44] *Ibid.*
[45] FSCA *Regulatory Strategy* 57.
[46] *Ibid.*
[47] FSB *CBR's Revised Categorisation* 2.
[48] FSCA *Regulatory Strategy* 41.
[49] *Ibid.*
[50] *Ibid.*
[51] *Ibid.*
[52] Treasury *Explanatory policy paper accompanying COFI* 11.
[53] *Ibid.*

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evolved and will continue to do so from the viewpoint of assessing whether financial institutions are conducting themselves in a manner that delivers the desired customer outcomes as opposed to assessing on compliance and prescriptive rule-based requirements.[54]

This approach has been supported by the ongoing requests from the FSCA for data through information gathering processes.[55] The historic requests remain, however the ability to detect conduct risks are not necessarily possible through the analysis of the regular report submissions.[56] This was the initial challenge and hence the need for change. The research indicated that there is no indication that this challenge has been addressed through a clear and publicized regulatory strategy setting out exactly how the FSCA aims to "do things differently" in line with the acknowledgement of the importance of complaints management for market conduct regulation. It is also clear from the analysis of the reports of the ombuds in chapter five, that the information provided by the ombud schemes is not helpful to determine where the issues that cause complaints originate (this is not determinable from noting which sectors are subject to the most complaints and highlighting generic complaints on a principled level).

Managing an organisation's risk and ensuring compliance with regulatory requirements has always fallen within the ambit of the compliance role.[57] With the changes which have taken place over the past three to five years, the question to be asked is whether the insurance industry still maintains the view that adherence to the changed market conduct rules and principles remain a compliance exercise. While the key areas are theoretical in that processes, frameworks, and governance structures ought to be in place, the practical application thereof requires a robust regulatory approach with stringent and intrusive oversight practices to ensure compliance.

There are three simplistic ways for an insurer, as a financial institution, to consider market conduct risk, its monitoring, and its effective management: determine who should be managing conduct risk within an insurer; determine how conduct risk can be managed effectively and determine what should be measured and monitored to ensure customers are receiving fair outcomes. This means that greater reliance will be placed upon a financial institution to initiate, change, and implement practices which are aligned to the market conduct principles. However, the Regulator will utilise the tools available to it from a regulatory and supervisory perspective

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[54] *Ibid.*
[55] *Idem* at 93.
[56] *Ibid.*
[57] See par 2.5 above.

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to establish how it will monitor and manage the respective financial institutions. A financial institution will therefore be expected to ensure that its processes, frameworks, and structures align to the regulatory requirements and that there is ongoing monitoring, reviewing, and an analysis of its data to detect and deal with any market conduct risks that may arise.

Notwithstanding the above, I doubt whether the FSCA has managed to achieve a level of oversight consistent with their articulated objectives as there is no differentiation between their approach towards complaints management, and other stages of the customer-institution relationship irrespective of how the various stages (and needs of consumers during these stages) differ.

The above raises a number of questions on the impact of the new regulatory and legislative structures on insurers as regulated entities. Does compliance become an expensive resource to the business? Will financial institutions be expected to expand on their compliance capability on an institution-wide level to ensure adherence to the regulatory requirements of market conduct? I am of the view that the responsibility extends to all aspects of the business in line with the cultural reformation envisaged by TCF. The compliance function remains unchanged; however, the business must now adapt to incorporate market conduct into its operational strategy to ensure that all levels of the business are aligned to the principles and expectations of market conduct. The costs thereof are yet to be determined.

The challenges (and confusion for those tasked with designing complaints management frameworks for insurers and ensuring compliance with the expectations of the regulator) continue:[58] The complaints management framework within the amended PPRs and the provisions within the COFI Bill are intended to provide clarity to financial institutions to ensure consistency and standardization in the process. The intention was to provide certainty to enable the regulation of conduct. The supposed introduction of the principles of fairness, equity and good faith deviated from the principles and strict application of the law of contract. The question that therefore begs to be answered is whether the amendments were now intended to incorporate these common law principles and public policy into the legislative regime. In addition, without some ability to gauge outcomes and consistency by the ombuds when it

[58] See par 3.6 above.

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comes to decisions based on norms such as fairness, it is difficult to foresee certainty on the side of the insurer.[59]

With this background, it becomes clear that the financial services industry is to be held to a higher standard when compared to other industries. Is this fair, considering that there are variations between the services offered or products being sold? There is risk to the customer, however, the customer, in an ideal scenario would be made aware of the risk prior to undertaking same. If there was a failure in terms of awareness, there ought to be a penalty against the financial institution for this failure. The current status quo appears to illustrate that the failure is established when the damage has already occurred and the customer has been prejudiced, thereby imposing financial hardship on a customer.[60]

As discussed,[61] there are primarily two types of insurance which is available to customers, that of long-term insurance and short-term insurance. The volume of complaints received and published by the ombudsman schemes is an illustration of the market conduct concerns and trends relating to the weakness of the controls.[62] Hence, the need to strengthen the oversight of market conduct within the financial services industry,[63] Within the long-term sector, the complaint trends illustrate that the penalties relating to early termination of retirement and other savings policies are extremely high. Based on an analysis of these complaints, regulations were passed to reduce these charges and limit the commission that would generally be paid upfront.[64]

On short-term, one of the greatest challenges from a market conduct perspective was particularly on credit insurance. The objective would be to protect customers who borrow and their dependents from their asset being repossessed in the event of a death or loss of income. Are the objectives being met? If they are, why would be there be a trend of complaints relating to these types of cover? Considering the landscape within the South African economy and the unemployment rate, this type of cover would be required. However, the market conduct trends which arise out of the complaints data received by the Regulator have raised concerns, which concerns will be reviewed to ensure that the objectives of the product are met and that there are no concerns from a customer point of view.[65] It is the writer's view that the concerns which

[59] See par 4.6 above.
[60] Treasury *A safer financial sector to serve South Africa better* 41.
[61] See ch 5 above.
[62] *Idem* at 44.
[63] *Ibid.*
[64] *Ibid.*
[65] *Ibid.*

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are identified provide the view that the customer is placed at a disadvantage due to the limited knowledge which it has in relation to the financial institution. Is the fear of the "big corporate" versus the "poor customer" mindset a reality? Does the Regulator have a valid concern in relation to the market conduct concerns that have been raised?

In the writer's view, there is "truth" to the concerns which have been raised. The various publications on complaints data as well as the enforcement actions taken are a clear indication that these are valid. However, the unfairness from a financial institution perspective is that there are financial institutions who incorporate and build market conduct practices into their daily operations where the customer is "at the heart" of the business. However, due to the behaviour of certain institutions, unfortunately, the rest of the financial institutions have to compensate accordingly.

The learnings arising out of Chapter 6 and the international markets is that a proactive approach is preferred to ensure the delivery of results in terms of suitable and fair outcomes to financial services customers. The issue is determining what a proactive approach is and being in a position to ensure that same is adequately implemented. The culture within the financial services industry is to ensure that all parties are aligned to ensuring the fair treatment of its customers, i.e. the regulator, financial institutions and a fair level of understanding by its customers in terms of what these expected outcomes ought to be. The aspects which were evident and consistent in both financial markets mentioned in Chapter 6 were the fact that financial institutions as well as regulators ought to be in a position to detect discrepancies through reporting, processes, engagements, feedback, data gathering and information requests. The detection is to be considered early warning mechanisms to assist in preventing unfair outcomes to financial services customers. Once detected, the information ought to be analysed to assess the risk and exposure to both the customer and business. Once understood, it is important to respond by making tough decisions, communicate, educate and ensure that guidance is provided. Continuous learning ensures continuous improvement. What is also important is being agile to adapt, when necessary to ensure effective and efficient ways of working.

With this being noted, we are to establish and determine whether a move away from a rules-based approach to a principles-based approach allow for standardization and compliance and its ease of achieving its objectives. The three themes which arise from this are the broad-based standards in preference to detailed rules; outcomes-based regulation and increasing the

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responsibility of senior management. Would the financial services industry take issue with the amendments to the PPRs in that they are too high level and do not provide adequate detail to establish compliance? Are the principles general? Principles have a number of characteristics, which include the fact that they are drafted at a high level of generality; with the intention of having overarching requirements that can be applied flexibly to a fast paced and changing industry; they contain terms which are qualitative and not quantitative; they can be applied broadly; they contain behavioural standards; a breach must have an element of fault; a breach can be sanctioned through public enforcement action. The intention of a more principles-based approach is that same allows for more flexibility, same is also more likely to produce behaviour which meets the intention of the regulator and allows for easier compliance. The detailed rules are intended to provide certainty; a clear standard of behaviour and are easier to apply consistently. However, there exists room for gaps, inconsistencies, rigidity and create creative compliance. Principles have the potential to engage senior management in the regulatory process; principles also focus more on the purpose as opposed to the actual rule. Principles offer flexibility; enhance responsiveness. They are also difficult to manipulate.

7.3. Conclusion

Through the research and an analysis of feedback from international markets, it has become apparent that the financial services industry, specific to complaints management in the insurance industry required a change. The change, in my view brought with it a need for greater engagement between the industry and the Regulator, an exercise of education for not just the financial services customer, but for the financial services institution, as well. The need for standardization and consistency was a requirement which was much needed. Whilst it is noted that there is a separate market conduct regulator, it is clear that there should be effective coordination to ensure a sustainable model in future. The balance between market conduct and prudential can create conflict.

The research seems to have raised a number of unanswered questions – not all of which fall within the ambit of legal scholarship (such as the cost-impact of the regulatory changes to complaints managements). In conclusion, the following areas were identified as key areas of concern within complaints management which will require constant monitoring, review and research in order to ensure that complaints management complement market conduct outcomes as envisaged: a non-generic focus on processes and the outcomes *unique to complaints management*; building strong relationships between financial institutions, its customers and the

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Regulator (and the ombud schemes); focusing on non-generic coordination of *useful* complaints management data coupled with *useful* feedback from the Regulator on whether its expectations for *complaints management* has been met (and considering the need for a balance between market conduct and prudential reporting); effective consultation and information sharing; and fostering a flexible framework, which allows for an agile and adaptable complaints management environment.

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