INSURANCE DIVISION

FUTURE APPROACH TO MARKET CONDUCT SUPERVISION

Farzana Badat
HoD: Insurance Compliance
(Market Conduct Supervision)
Insurance Regulatory Seminar
2 November 2015/ 5 November 2015

FSB

INSURANCE DIVISION

Agenda

- INCREMENTAL APPROACH TO IMPLEMENTATION OF TCF
- FUTURE APPROACH TO MARKET CONDUCT SUPERVISION
- KEY CURRENT AND FUTURE SUPERVISORY FOCUS AREAS
- GENERAL OBSERVATIONS

FSB

INSURANCE DIVISION

RECAP: Twin Peaks

MARKET CONDUCT (protection of financial customers)
- Fair treatment of customers
- Market efficiency & integrity
- Consumer education

FSCA
Financial Sector Conduct Authority

PRUDENTIAL (financial soundness of institutions)
- Product providers (esp. banks and insurers)
- Market infrastructures
- Financial conglomerates

Prudential Authority (within SARB)

FINANCIAL STABILITY (protect and enhance system-wide stability)
- Monitor & mitigate stability risks
- Financial Stability Oversight Committee
- Resolution authority

SARB

INCREMENTAL APPROACH TO IMPLEMENTATION OF TCF

INSURANCE DIVISION

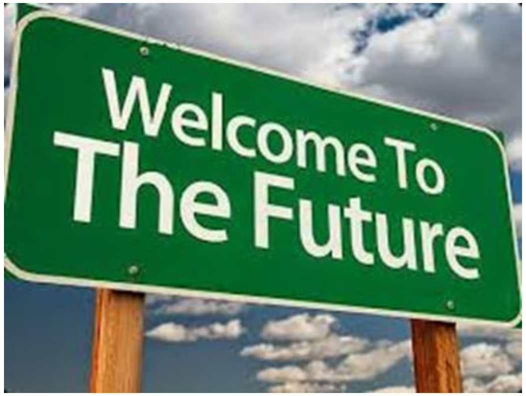
The future – From FSB to FSCA

- **FSB → → →FSCA –** responsible for future market conduct supervision

- BUT: Has the "future" not arrived?

- REMEMBER: Consistent message from the FSB re: *"Incremental implementation of TCF"*

- Move from <u>talking</u> about TCF outcomes to <u>proactive management</u> of market conduct risks



INSURANCE DIVISION

INSURANCE DIVISION

Incremental implementation of TCF

- **What does *"incremental implementation"* mean?**

CURRENT SUPERVISION

  - Challenging TCF commitment when investigating concerns
  - Testing of TCF commitment and culture – focus on effectiveness of operational implementation
  - Identifying market conduct risk indicators
  - Specific thematic supervisory initiatives testing risks to fair customer outcomes

  - Structured reporting on market conduct risk indicators
  - Reviewing existing regulatory frameworks to test whether they support fair customer outcomes
  - Introducing TCF principles into existing regulation
  - Reflecting TCF principles into overarching Twin Peaks regulatory framework

FSB

INSURANCE DIVISION

FUTURE APPROACH TO MARKET CONDUCT SUPERVISION

INSURANCE DIVISION

Future Guiding Principles

- Regulation and Supervision must be:
  - transparent
  - comprehensive and consistent
  - **intensive and intrusive**
  - **outcomes based** (TCF, market integrity and other policy outcomes)
  - **risk based and proportional**
  - **pre-emptive and proactive**
  - a credible deterrent
  - aligned to applicable international standards

FSB

INSURANCE DIVISION

Cross-cutting activity-based focus

- Culture and governance
- Product value
- Unfair contract terms
- Misleading advertising/marketing
- Ineffective disclosure
- Conflicted advice
- Poor claims handling
- Poor complaints handling
- Empowered customers

Testing outcomes, rather than compliance 'tick-box'

Rebalancing of responsibilities: Increased scrutiny of the way firms develop products;

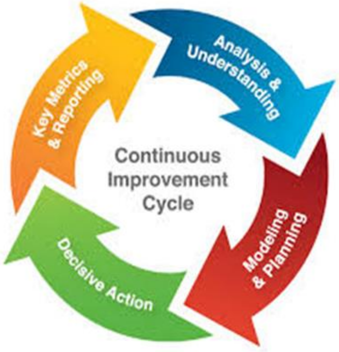
Product provider oversight of chosen distribution channel

Fair outcomes can be achieved in different ways, through emphasising different TCF elements

INSURANCE DIVISION

Supervisory expectations

- Ongoing, proactive, demonstrable management of conduct risk indicators manifesting in:
  - Continuous improvement in product design, service delivery, customer experience
  - Fair pricing
  - Appropriate products
  - Clear and understandable disclosures
  - Improved claims handling practices
  - Reduction in persistent complaints
  - Meaningful management information and reporting
  - Enhanced governance and oversight of distribution channel
  - Customer centric decision making



FSB

INSURANCE DIVISION

Using data to demonstrate value

- Meaningful regulatory and management reporting requires consolidation of accurate, quality and usable data from various distribution touch points

- Investing in more reliable, dependable, quality data helps to articulate conduct risks more precisely and makes compliance much easier to **demonstrate**

- Having consistent access to the right data, in the desired format and at the right moment helps to generate new insights for better customer solutions and improved business efficiencies

Reference:

Data Points: HOW FINANCIAL SERVICES FIRMS USE TECHNOLOGY TO TURN DATA INTO ACTIONABLE INSIGHT
Bloomberg for Enterprise

INSURANCE DIVISION

KEY CURRENT AND FUTURE SUPERVISORY FOCUS AREAS

Current and future focus areas

- Binders/ Outsourcing (LT&ST)
- Claims Thematic Review (LT&ST)
- Complaints Management (LT&ST)
- Quarterly Market Conduct Meetings (LT&ST)
- Conduct of Business Reporting (LT&ST)
- Premium reviews (LT)
- “Moving” of policies (LT&ST)
- Tax Free Savings Accounts (LT)
- Other supervisory initiatives

INSURANCE DIVISION

Binders/ Outsourcing

- Observations and supervisory expectations

- Outsourcing to improve efficiencies and in the interest of policyholders

- Governance and oversight – upfront and ongoing

- Remuneration – being considered under RDR

- Data exchange
  - Frequency
  - Quality
  - Integrity
  - Security
  - Usability

- Industry Data Specification – Mandatory fields

- Insurers of concern – require independent "audits" to demonstrate operational capability

INSURANCE DIVISION

FSB

INSURANCE DIVISION

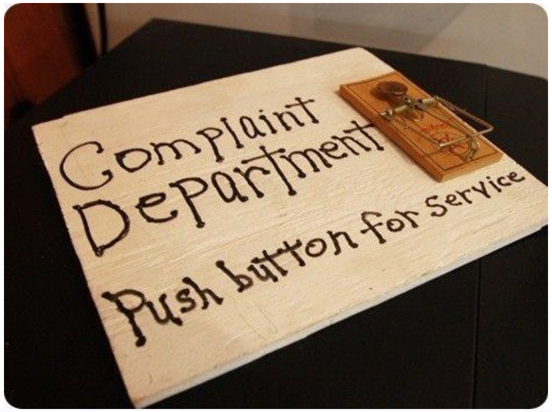
Claims Thematic Review

- 14 insurers identified
- Risk-based
- Focus areas:
  - Structure, resourcing and remuneration
  - Governance and oversight
  - Claims submission process
  - Assessment of claims
  - Management of fraud risk
  - Settlement of claims
  - Repudiation processes
  - Link to complaints
  - Overall TCF embedment

- Observations to date:
  - Inconsistent definitions of "claim", "repudiation", "rejection" and capturing of information
  - Client experience – inconsistent measuring of turnaround times, lack of feedback
  - Underwriting at claims stage

Complaints Management

- 2014 Thematic Review Follow Up
- Information Letter 3 of 2014 – Key Findings and Supervisory Expectations
- Monitoring of Ombudsman Statistics
- Focus areas
  - Root cause analysis and quality of management reporting
  - First call resolution and escalation processes
  - Link to business continuous improvement processes
  - Proper categorisation
  - Monitoring at distribution level



INSURANCE DIVISION

FSB

INSURANCE DIVISION

Quarterly Market Conduct Meetings

- Risk based, proactive and regular interactions with senior management

- Better understanding of business models

- Sharing of information

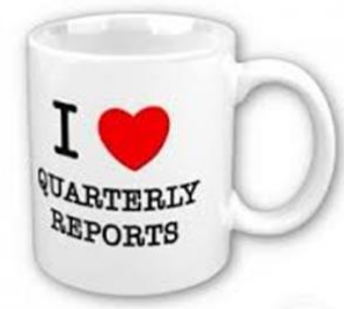
- Focus areas:
  - Key business highlights and significant developments
  - Governance and oversight of conduct risk issues
  - Complaints and claims trends analysis
  - New product launches and/or campaigns
  - Updates on supervisory initiatives
  - General regulatory and business concerns

INTENSIVE
&
INTRUSIVE

INSURANCE DIVISION

Conduct of Business Reporting

- Proposed quarterly reporting on key conduct risk indicators
- Second draft being finalised for comment and testing
- Alignment to SAM authorisation classes and Insurance Bill definitions
- Data required per distribution channel
- Focus areas:
  - Quantitative sales and premium information
  - Details of benefits, including VAPs
  - Not Taken Up, Policy Paid Up, Replacement, Surrender and Lapse Rates
  - Details of remuneration – Commission, Binder, Outsourcing and Other Fees
  - Detailed claims information
  - Detailed complaints information
  - Marketing spend



FSB

INSURANCE DIVISION

Premium Reviews

- Investigation initiated in response to complaints of deliberate mispricing/ excessive premium increases on certain life risk products
- Discussions held with senior management and Board members of 5 insurance groups
- Example of interconnectedness between actuarial decisions and consideration of conduct risks, fair balance between interests of shareholders and policyholders
- Focus on the role of actuarial oversight structures in assessing risks to fair customer outcomes
- Report and guidance to be issued on application of TCF considerations when making significant pricing decisions
- Focus on Board oversight, appropriateness of pricing decisions, clear ongoing communication, options to policyholders

Moving of policies

- Investigation into industry practice of “bulk” movements of policies -18 insurers identified

- Summary of concerns:
  - Inadequate incorporation of TCF considerations when moving policies
  - Reliance on “negative” consent
  - Insurers unable to provide data on policies moved over the past two years
  - Inconsistent adherence to 30 day policyholder notification rule
  - Lack of insurer oversight over intermediary communication with policyholders relating to policy terminations

- Some actions to date:
  - Follow up with individual insurers on specific concerns
  - Closer scrutiny of Directive 151 submissions
  - Input into draft information letter on cancellation of policies
  - Input into RDR proposal relating to cover cancellations
  - Findings shared with FAIS Division

INSURANCE DIVISION

FSB

INSURANCE DIVISION

Tax Free Savings Accounts

- Example of cross-cutting supervisory focus area

- Regulations in terms of section 12(T)(8) of the Income Tax Act, No. 58 of 1962:
  - Published on 25 February 2015 and effective 1 March 2015
  - To enable providers of financial products to market and distribute tax free savings products in order to encourage household savings

- Section 12T(9) grants the FSB the mandate to supervise and enforce compliance with the Regulations

- Objectives:
  - Address low level of household savings in the country
  - Provide tax free savings products that are:
    - Simple to understand
    - Offered in a transparent manner
    - Carry fees and charges that are reasonable
    - Suitable for this target market, not necessarily expert investors

INSURANCE DIVISION

Tax Free Savings Accounts

- The following entities may issue and/or administer tax free savings products:
  - Long-term Insurers as defined in the Long-term Insurance Act, 1998
  - Banks as defined in the Banks Act, 1990/ Mutual Banks Act, 1993/ Co-operative Banks Act, 2007
  - Managers of Collective Investment Schemes as defined in the Collective Investment Schemes Control Act, 2002
  - National Government (retail savings bonds)
  - Authorised users in terms of the Financial Markets Act, 2012 (stock brokers)
  - Administrative (Cat III) FSPs in terms of the FAIS Act, 2002 (advisors/ intermediaries)

Tax Free Savings Accounts

- Establishment of FSB cross-cutting supervisory working group
- Focus areas:
  - Development of supervisory framework
  - Dealing with technical queries and complaints
  - Engagement with National Treasury and SARS
  - Entity level product supervision
- Centralised contact point: FSB.TaxFreeSavings@fsb.co.za

FSB

INSURANCE DIVISION

INSURANCE DIVISION

Tax Free Savings Accounts

- Contribution limits:
  - Annual – R30 000
  - Lifetime – R500 000

- Observations and concerns to date:
  - Clarity of disclosures
  - Monitoring and tracking of over contributions
  - Complexity and suitability of products
  - Calculation of fees
  - Ability of providers to effect transfers between accounts

FSB

INSURANCE DIVISION

Other supervisory initiatives

- Travel Insurance (ST)
  - 5 insurers identified
  - Inconsistent remuneration structures
  - Concerns regarding premium collection
  - Policy wordings not always easy to understand
  - Lack of insurer oversight
- Value Added Products (ST)
  - Require more focus on product suitability and demonstrating value to clients
  - Analysis of specific offerings such as roadside assistance and extended warranties
- Consumer Credit Insurance (LT&ST)
  - Concerns relating to product suitability, distribution and pricing
  - Detailed information request imminent
- Multiple Causal Event Charges (LT)
  - Concerns relating to timeous compliance with Directive 153
  - In depth industry investigation imminent

GENERAL OBSERVATIONS

INSURANCE DIVISION

A few closing thoughts

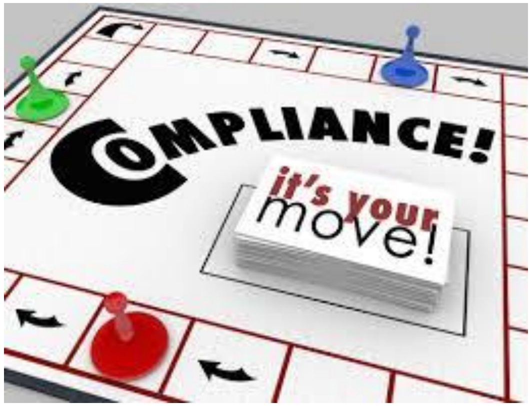
- Insurer resolution of complaints received by the FSB:
  - Insurers with demonstrable commitment to customer-centricity more likely to reach fair resolution
  - Quality of responses to complaints may be an indicator of level of commitment and overall culture
  - FSB versus Ombudsman focus areas – intervention only if residual conduct concerns arise, specific regulatory non-compliance is identified or there are indicators of possible broader policyholder impact
- Board and senior management consideration of market conduct risks
  - Consideration of customer impact in strategy setting and business planning
  - Evidence in minutes of Board discussions and integration in overall enterprise risk management framework
  - Ensure reporting across operational areas and limit over reliance on “TCF” reporting from compliance function only

FSB

INSURANCE DIVISION

Remember…

- No more “**just talking**” about TCF
- **Demonstrate** proactive management of conduct risks across value chain
- Manifesting in **continuous improvement** to products, delivery and overall experience
- Resulting in **better outcomes** for customers
- And finally . . .
  - It’s all about that **DATA**!



INSURANCE DIVISION

Questions?