



national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA



Financial Sector
Conduct Authority

Treating Bank Customers More Fairly:

Invitation to comment on the South Africa Retail Banking Diagnostic

National Treasury and the Financial Sector Conduct Authority (FSCA) today publish for public comment a diagnostic study prepared by the World Bank aimed at ensuring fairer bank practises in South Africa. The report is titled “*South Africa Retail Banking Diagnostic: Treating Customers Fairly in relation to Transactional Accounts and Fixed Deposits*”.

This study represents the first step in improving market conduct practices in the banking sector, to ensure that bank customers are treated more fairly than in the past. The study was commissioned by National Treasury to provide independent research on identifying the extent to which banks treat their retail customers fairly in relation to transactional and fixed deposit accounts. The findings should not be seen as applying to any specific bank or all banks equally. The treatment of customers varies from one bank to another as well as by product offering.

The study’s analysis and recommendations, as well as public comments on the study, will help shape the FSCA’s approach to regulating the way banks treat their customers, an approach which is currently being developed. It will contribute to a stronger market conduct regulatory framework in the financial sector. The findings and the variations in approach by banks point to the need for clear and consistent standards of customer treatment.

Fair treatment refers to, among others:

- the appropriate design of products and services that meet customers’ needs;
- the provision of clear information to customers at the point of sale;
- ensuring that products perform as customers have been led to believe; and
- ensuring customers are able to submit complaints and disputes, and have these resolved

The diagnostic study identifies potential shortcomings in bank conduct at each of these stages, and makes recommendations. The findings are deemed to be potential

shortcomings because while the conduct of banks is not necessarily in breach of legislation or regulations, it may fall short of fair treatment principles and international best practice (or experience). The study will help ensure that regulation is evidence-based, for a financial sector that is stable, fair, and inclusive.

The study is written as an 'exception report' – it identifies potential shortcomings in the conduct of banks, rather than also focusing on good practices that do not require intervention. Some high level findings include:

- Complex product design that makes it difficult for customers to compare products;
- Potentially unfair terms and conditions;
- Potentially unfair fees;
- Wide variation in what, when, and how information about product features and pricing is disclosed; and
- Gaps in regulation, and inconsistencies in how regulation is applied.

Recommendations to address issues identified include:

- Introducing new obligations on financial institutions to ensure their processes for developing, and making changes, to account and deposit products focus on product suitability for customers;
- Considering new measures to promote the provision of transactional accounts that respond to the needs of low-income customers, including in terms of cost and value;
- Having an effective regime to prohibit unfair terms and fees for account and deposit products; and
- Implementing an improved disclosure regime to ensure that account and deposit product customers are provided with timely, clear and comparable information by all institutions.

Background

The diagnostic study is the latest in a number of developments regarding the regulation of the banking sector in South Africa. The Banking Enquiry of the Competition Commission published its final report in 2008¹. The Enquiry (also known as the Jali Commission) focused on competition issues in the South African banking sector, but its final report also made a number of findings and recommendations in relation to poor outcomes experienced by the customers of retail banks. While most of the recommendations of the Banking Enquiry have since been implemented, the Enquiry's findings highlighted a gap in the regulation of the market conduct of retail banks.

This gap was in part due to the strong focus then on prudential regulation through the Banks Act, then overseen by the South African Reserve Bank (SARB). The jurisdiction of the Financial Services Board (FSB) – a non-bank regulator with a mandate that included both prudential and conduct regulation – did not extend to the banking sector, other than

¹ Available on <http://www.compcom.co.za/banking-enquiry/>

to the extent that banks' financial intermediation activities were subject to the Financial Advisory and Intermediary Services Act (Act 37 of 2002). The National Credit Regulator has jurisdiction over the conduct of retail banks, but only in respect of the provision of credit in terms of the National Credit Act (Act 34 of 2005).

The Financial Sector Regulation Act (Act 9 of 2017) gave effect to a new financial sector regulatory model in South Africa – the Twin Peaks model. Through the Act, two new regulators were established on 1 April 2018 – the Prudential Authority within the SARB and the FSCA, which replaced the FSB. The FSCA is established as a dedicated market conduct regulator, with full jurisdiction over all financial institutions in South Africa.

This means that the market conduct of banks in South Africa will be directly regulated for the first time.

The technical assistance for this diagnostic study has been provided as part of the South Africa Financial Sector Development and Reform Program (FSDRP) undertaken by the World Bank Group and supported by the Swiss State Secretariat for Economic Affairs.

Financial inclusion

Also published today for reference purposes is a 2016 report by the World Bank, "*Achieving Effective Financial Inclusion in South Africa: A Payments Perspective*." This report examined factors that influence access to and use of transactional accounts and electronic payment instruments. It also made several recommendations on how new businesses with innovative offerings can enter the market. This report has since been used by the National Treasury and SARB to inform policy and regulatory developments regarding payment system regulation. It will also feed into Government's financial inclusion policy approach, details of which will be released in the near future.

The 2016 report had not been publically released. It is now being published as a reference document to the retail banking diagnostic study, which does not cover issues already addressed in the 2016 paper, but which makes reference to the 2016 paper where relevant.

It is emphasised that information and recommendations in the 2016 paper may have since been overtaken by the work underway by National Treasury and various regulators in relation to payment system regulation. Therefore, no comment is sought on this paper.

Comment submission

Comments on the diagnostic study are invited until 16 October 2018. Comments can be sent to marketconduct@treasury.gov.za

The National Treasury and FSCA will also schedule workshops on the report and its recommendations to support engagement. Detail on these workshops will be communicated in due course.

---ENDS---

ANNEXURE A

Summary of recommendations of the South Africa Retail Banking Diagnostic

Area	Recommendation
Product design recommendations	
Transactional accounts for low income customers	<ul style="list-style-type: none"> • The South African authorities should consider strengthening, and simplifying, the reporting parameters under the FS Code regarding transactional accounts to more clearly incentivize banks to ensure that pricing as well as features support accessibility. • The South African authorities should also consider introducing measures, such as introduced through regulation in the European Union for example, or through a coordinated industry agreement in Canada, promoting the provision of full featured transactional account offerings that respond to the needs of low income customers, including in terms of pricing. Consideration should be given to setting out minimum feature and pricing aspects to be met, but which providers could then enhance / build on, fostering accessibility while allowing for innovation. Importantly, the parameters of any such intervention should be based on comprehensive customer-focused research that examines in sufficient detail not only low income individuals' current usage in South Africa, but also broader financial transaction needs, behaviors, preferences and related physical and technological accessibility (e.g. drivers for continued demand for branch and ATM access and cash usage). Research should also have regard to potential market impact, including previous experience and concerns expressed with regard to Mzansi accounts. • In addition, the general product design obligations recommended below should apply to all levels of product offerings, including low income products.

<p>Middle income transactional account offerings</p>	<ul style="list-style-type: none"> • The COFI/FSR Laws should include specific product design obligations to ensure that financial institutions' processes for developing, and making changes to, transactional account (and fixed deposit) products comprise clear, concrete steps intended to drive TCF Outcomes. Examples of approaches are provided in the report. At least initially, such obligations should be principles-based, particularly assuming that they would not be confined to transactional accounts and fixed deposit products but would also be intended to apply to other financial products. Importantly, however, the FSCA should augment such principles-based obligations by issuing more detailed regulatory guidance, addressing product-specific practicalities and concerns (that can be updated over time reflecting its supervision outcomes). If industry does not meet relevant expectations sufficiently then more prescriptive requirements could follow. • The South African authorities should, in addition, consider undertaking an updated Banking Enquiry style 'costs vs pricing' analysis and undertaking a complementary in-depth customer study regarding middle income customer switching behavior and attitudes.
<p>Fixed deposit design</p>	<ul style="list-style-type: none"> • The South African authorities should implement the specific product design obligations noted above to apply to fixed deposits, as well as the improvements to product disclosure discussed below.
<p>Potentially unfair product terms</p>	<ul style="list-style-type: none"> • A regime that would prohibit unfair terms in transactional account and fixed deposit standard form contracts should be implemented in the COFI/FSR Laws. The regime should provide both for enforcement by the FSCA and reliance by individual retail customers. The regime should contain appropriate adjustments for issues relating to financial products, such as regarding its application to pricing. The FSCA should issue upfront guidance on its expectations in this regard, which should include practical guidance focusing on the application of the regime to key aspects of financial products, such as unilateral rights of variation and exclusions of liability. Institutions should then be expected to undertake (e.g. during a transition period) substantive reviews and, where necessary,

	amendments, of terms and conditions to ensure consistency with the regime.
Product offer and sale	
Advertising and sales material	<ul style="list-style-type: none"> • The COFI/FSR Laws should explicitly and comprehensively address advertising and marketing practices in relation to transactional accounts and fixed deposits as outlined in the report (including to address existing legal gaps).
Product disclosure	<ul style="list-style-type: none"> • The COFI/FSR Laws should: <ul style="list-style-type: none"> ○ establish a disclosure regime for transactional accounts and fixed deposits that covers key features, terms, pricing, and rights and recourse for transaction and fixed account deposit products, as well as the manner and timing of disclosure. Flexibility for key contractual disclosures to be made in electronic format should be included; ○ require provision of a standardized short form disclosure document to summarize key product features, pricing, and terms and conditions of transaction and fixed deposit accounts. (The report discusses the content and provision of such documents in detail, including availability through all applicable channels and the need for verbal explanations in some circumstances). • The South African authorities should establish standards for disclosing and explaining interest rates and calculation of interest on fixed deposits in a simplified manner. • The South African authorities should give careful consideration to including an overall cost indicator (based on standard / sample usage patterns) in short form disclosure documents for transactional accounts, or at least specially targeted categories. • The COFI/FSR Laws should mandate more comprehensive language requirements for key customer-facing documentation related to transactional accounts and fixed deposits reflecting approaches taken in and, importantly, lessons learned from, the implementation of such requirements in the National Credit Act and, for the public sector, the Use of Official Languages Act. • The authorities should establish or support the establishment of a centralized website and related tools that facilitate easy product comparison on comparable

	<p>features and prices of transactional accounts and fixed deposits.</p>
<p>Advice and sales practices and incentives</p>	<ul style="list-style-type: none">• Building on the approaches taken in the FAIS Legislation with respect to sales practices, the COFI/FSR Laws should appropriately strengthen governance of advice and sales related to transactional accounts and fixed deposits, including regarding:<ul style="list-style-type: none">○ compensation of frontline sales staff and agents to limit consumer risks;○ protective rules governing relationships between banks, third-party agents/intermediaries and retail customers (leveraging work so far under the Retail Distribution Review).• Importantly, the application of these rules should be proportional, and adaptable, to initiatives intended to promote effective access by low income consumers to transaction and savings products.

Product operation and administration	
Potentially unfair fees	<ul style="list-style-type: none"> • The regime prohibiting unfair terms recommended above should apply to relevant fees. The fairness of such fees would then be tested against the restrictions in the regime to determine whether the fee is appropriate. • If necessary (depending on the implementation of the regime) the application of existing legislative and common law doctrines on penalties should be clarified for financial sector participants. • The disclosure improvements recommended above should also be pursued to address the potential lack of customer awareness regarding the application of relevant fees. Such fees should not be enforceable unless disclosed consistently with new disclosure requirements
Dormant transactional accounts	<ul style="list-style-type: none"> • South African authorities should issue specific regulatory requirements on transparency and fair conduct related to dormant accounts, including defining the time or circumstances when an account would be considered dormant, to ensure uniformity of customer treatment by banks, and parameters for: <ul style="list-style-type: none"> (i) identification of dormant accounts; (ii) notification to consumers; and (iii) closure. • Specific prohibitions of adverse practices should also be considered, such as continuing to charge maintenance fees on dormant accounts that have reached a zero or negative balance.
Temporary overdrafts / 'shadow' credit limits	<ul style="list-style-type: none"> • While recognizing that temporary overdrawing can serve a legitimate customer purpose, the South African authorities should consider how to best regulate it (e.g. whether it is necessary to amend the National Credit Act or National Credit Regulations to extend it more clearly to such facilities, or impose requirements through the COFI/FSR Laws) to ensure that banks do not engage in unfair practices in relation to temporary overdrawing of transactional accounts. More specific product design obligations of the kinds recommended above would also be relevant in ensuring that the inclusion of such features in transaction accounts is consistent with TCF Outcomes. • In the meantime, the NCR should also consider a targeted review of banks' current practices relating to temporary credit provided in connection with

	<p>transactional accounts to ensure compliance with the National Credit Act and National Credit Regulations</p>
Changes to terms and conditions and fees and charges	<ul style="list-style-type: none"> • The COFI/FSR Laws should mandate minimum notice periods and require individual customer notice of changes that will have a direct customer impact and having regard to the likelihood that a customer may not become aware of general public notices of relevant changes. • Unilateral variation rights included in terms and conditions should also be subject to an unfair terms regime as recommended above.
Statements	<ul style="list-style-type: none"> • The COFI/FSR Laws should specify requirements for the provision of periodic statements for transactional accounts. Regulatory requirements should address minimum content and format requirements, as well as frequency, timing, and manner of delivery (including making appropriate provision for easy access to statements, and other transactional information, through electronic channels).
Information about external dispute resolution	<ul style="list-style-type: none"> • The disclosure requirements recommended in the report should require banks to clearly disclose the contact information and basic processes for internal and external complaints handling mechanisms
Product closure and mobility	
Potential barriers to account closure	<ul style="list-style-type: none"> • The new disclosure requirements recommended above should cover inclusion of clear information regarding closure and switching rights and processes. • The authorities should work with the banking industry to achieve a common and facilitative industry approach to transferring bank accounts, including debit orders (before considering regulatory intervention).
Account switching processes	
Early termination and rollover of fixed deposits	<ul style="list-style-type: none"> • The short form disclosure documents that are recommended to be introduced above should provide a brief, clear explanation of the consequences of early termination, and of the implications at maturity if the customer does not withdraw the fixed deposit. • Potential inappropriateness or unfairness of terms governing early withdrawals should also be addressed through the product design and unfair terms measures referred to above. • A coordinated industry approach should be considered for providing alerts ahead of the maturity date of fixed deposits.
Code of Banking Practise	

<p>The report recommends in various instances addressing objectives reflected by the TCF Outcomes through legislative reforms but the CBP also remains a key document governing and influencing bank practices in relation to transactional accounts and fixed deposits. Several banks suggested that the CBP should be reviewed and further updated in the light of TCF Outcomes and the report notes some examples where it may currently have gaps or inconsistencies in this regard.</p>	<ul style="list-style-type: none">• The CBP should be reviewed to ensure that it fully reflects the latest public and regulatory expectations in the context of the TCF Outcomes.• Efforts should be made to enhance consumer awareness of the CBP.
----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------