A known and trusted ombuds system for all

Workshop on proposals set out in the consultation policy document on financial sector ombud system reforms

National Treasury | 29 November 2017

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Background

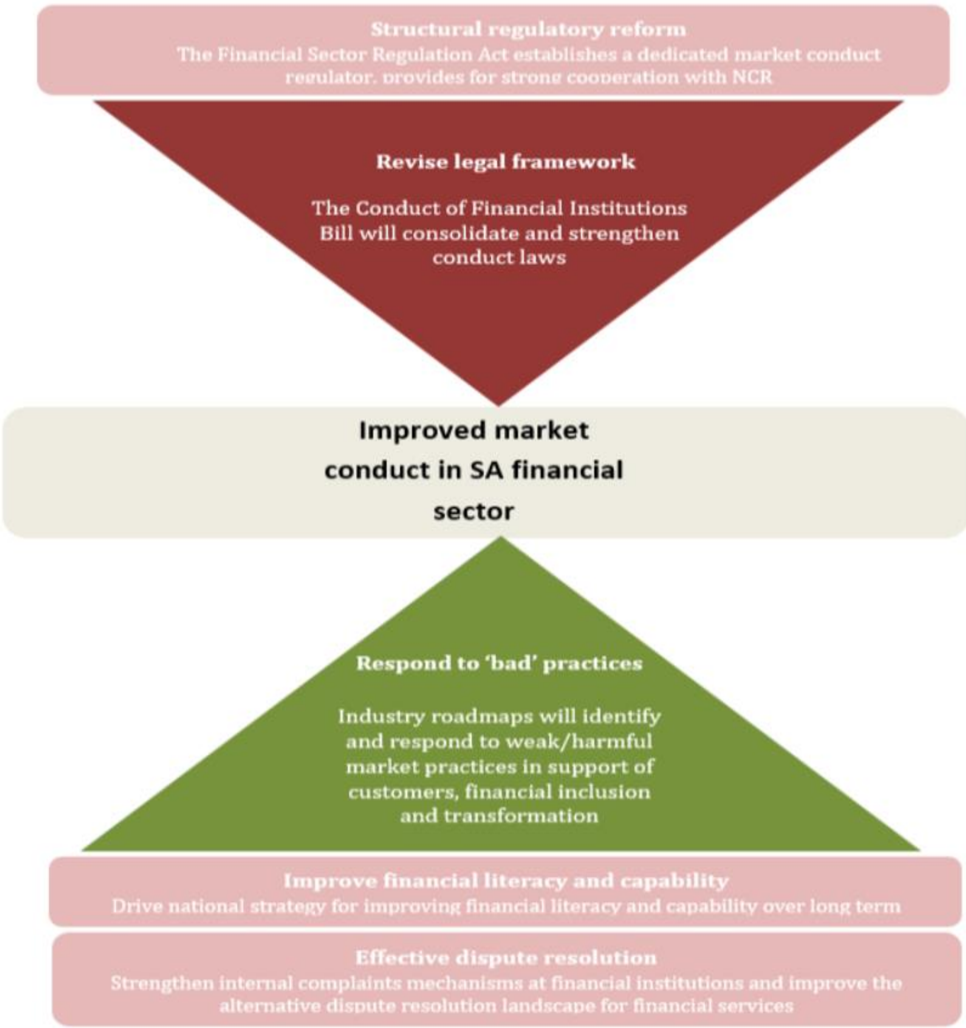
- The 2011 policy document "***A safer financial sector to serve South Africa better***" set out the need to strengthen financial sector regulation and ensure that the financial sector is serving South Africans better, particularly in terms of customer outcomes.

- The Twin Peaks reforms place dedicated emphasis on **strengthening market conduct regulation** in the financial sector, improving the fair treatment of customers. The FSR Act (Act 9 of 2017) creates a dedicated and stronger market conduct regulator, with full scope of jurisdiction over the financial sector - the FSCA.

- As identified in the 2014 discussion document, ***"Treating customers fairly in the Financial Sector: A draft market conduct policy framework for South Africa,"*** a strong consumer protection framework also requires an **effective, accessible and efficient alternative dispute resolution mechanism** for the financial sector.

- Improvements to the overall efficiency and effectiveness of the ombuds system is thus a focus area of the Twin Peaks reforms.

Policy approach being taken to strengthen market conduct



Ombuds system reforms

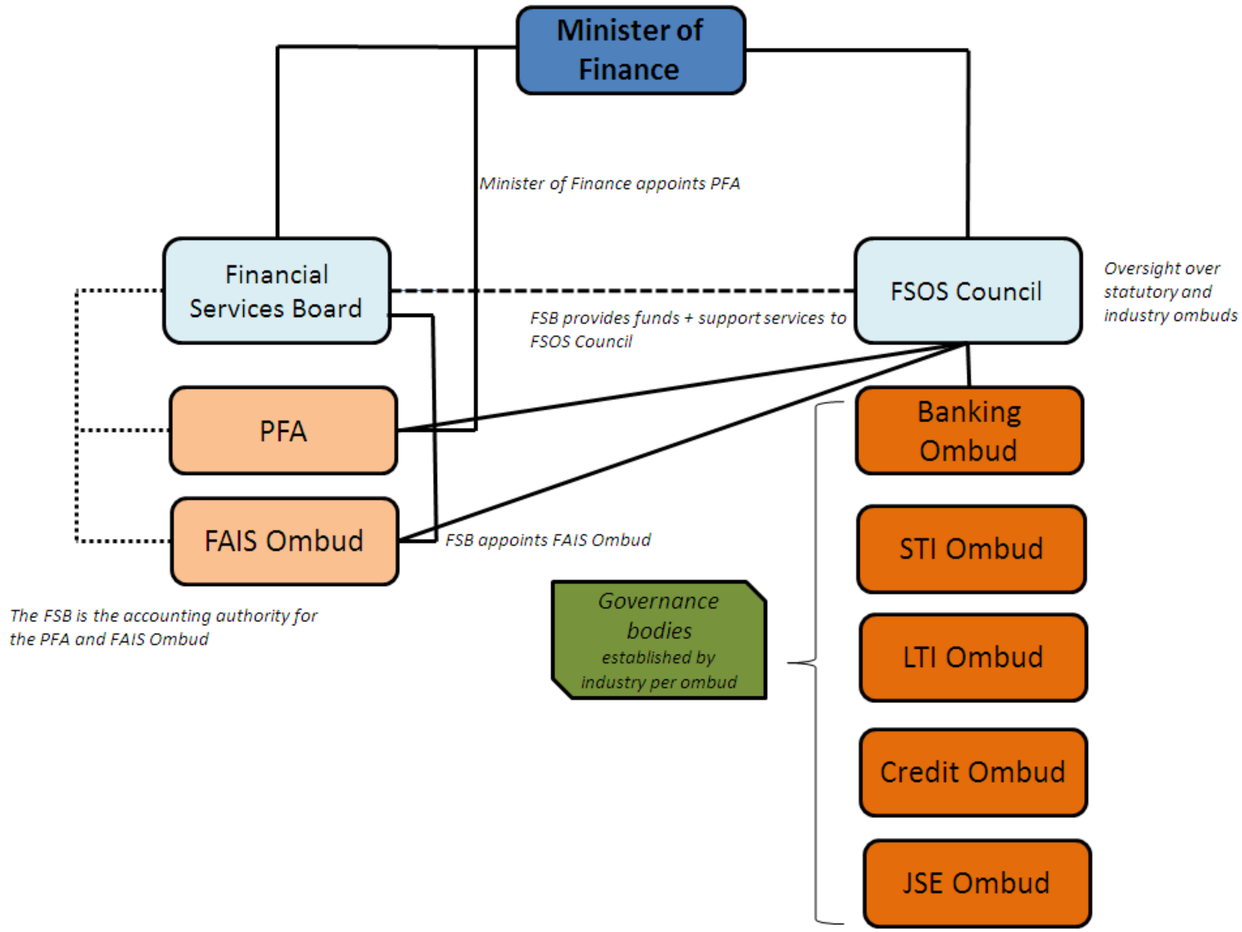
Ombuds in South African financial sector: Current framework

- South Africa has a mix of statutory and voluntary ombud schemes, which are institutionally-established, reflecting the current financial sector legislative environment:
  - **Voluntary ombuds**: Long Term Insurance, Short Term Insurance, Banking, Credit
  - **Statutory ombuds**: FAIS Ombud, PFA

- Ombuds are governed by the Financial Services Ombud Schemes Act of 2004 (FSOS Act). Voluntary schemes are recognised by the FSOS Council in terms of that Act

- The ombuds schemes have provided a vital channel for dispute resolution for financial customers dissatisfied with their financial services providers. However, the system has also experienced challenges, including:
  - **Relatively low awareness and access** (e.g. size of the market relative to complaints received and resolved)
  - **Gaps in coverage and jurisdictional inefficiencies** (contributing to customer uncertainty on which ombud to approach)
  - **Differences/inconsistencies in approach amongst the ombuds** (e.g. length of time to resolve dispute, amount that can be adjudicated on, etc.)
  - **Difficulties in measuring performance** – different governing structures, reporting periods, reporting requirements, funding arrangements

Current financial sector ombud scheme framework



Ombuds in South African financial sector: Current framework

- The FSOS Council, established through the FSOS Act, is intended to provide a level of oversight over the operations of ombuds systems. However, as a part-time structure with little power, it hasn't proved effective in streamlining ombuds operations.

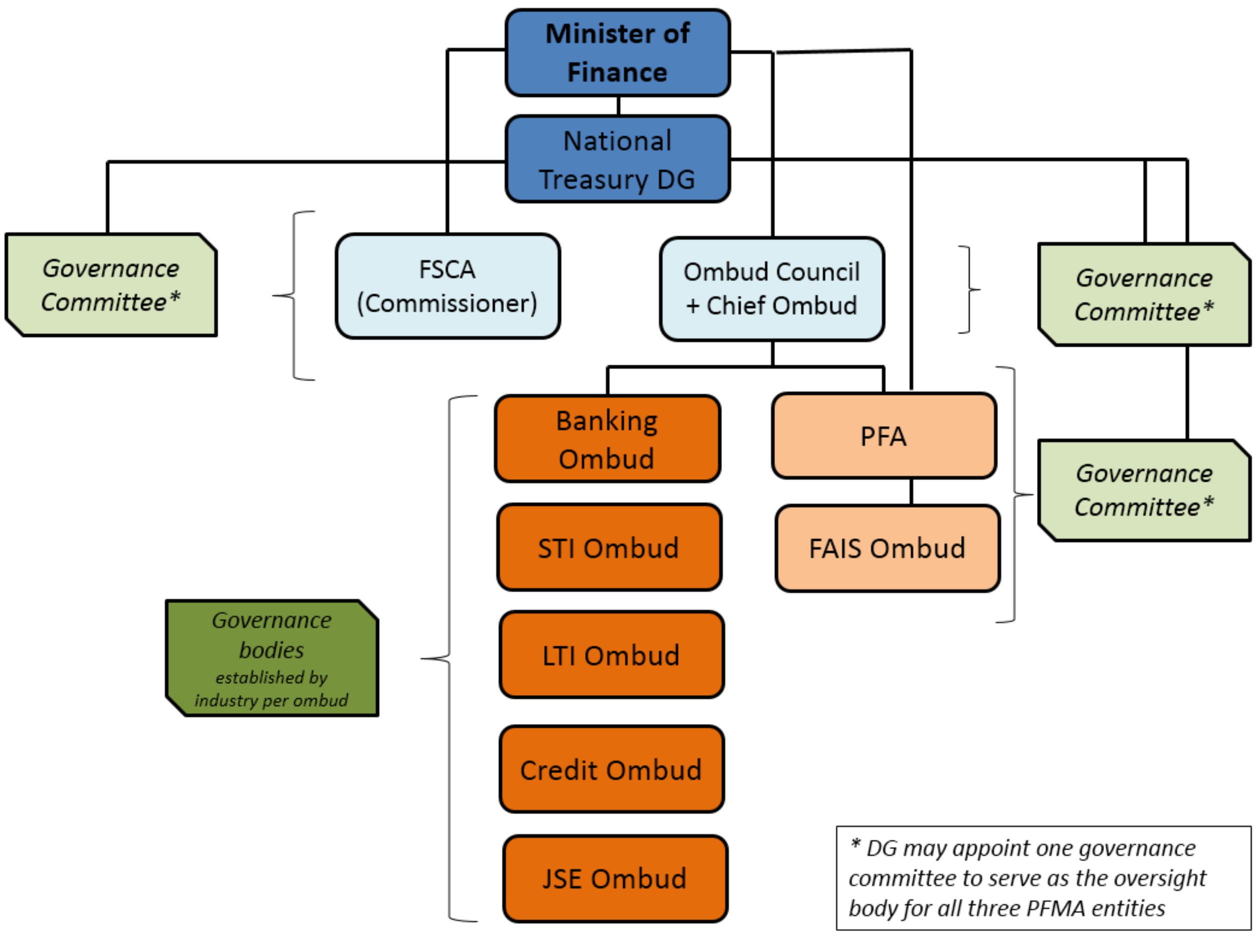
- A 2007 FinMark Trust report recommended **structural changes** to South Africa's alternative dispute resolution environment to promote the financial sector working better, particularly for lower-income consumers.

- The regulatory reforms underway as the financial sector shifts toward a Twin Peaks model provides the opportunity to consider improvements to the ombuds system in South Africa:
  - The creation of a new regulator to replace the FSB will result in the **FSB Board being dissolved**. Keeping in mind the oversight and funding role played by the Board with respect to the FSOS Council, PFA and FAIS Ombud, it becomes necessary **to consider which agency will perform this role going forward**
  - The intention to shift away **from institutionally-based regulation toward a more activity-driven legislative environment** also necessitates consideration of how the ombuds system will be impacted (e.g. proposed COFI Bill for market conduct regulation)

Twin Peaks reforms and the ombud system in South Africa

- The FSR (Act 9 of 2017) takes the first steps toward improvements in the ombuds system:
  - It **replaces the FSOS Council with a full-time Ombud Council**, which will be required to promote awareness, accessibility and use of the ombuds system, and take steps to improve its effectiveness, including by imposing common standards of best practice and promoting cooperation and coordination amongst ombuds.
  - The Ombud Council will be a full-time structure, headed by a **Chief Ombud**, with staff. It will be able to **take enforcement action for non-compliance** with rules set on ombud schemes.
  - The Ombud Council will establish a **single point of entry** into the ombud system.
  - The Act provides for **coverage of all financial product and financial service providers by appropriate ombud schemes**, including by requiring financial institutions to be a member of an industry ombud scheme operating for its sector
  - It **clarifies relationships** between the Ombud Council, ombuds, financial institutions and the Financial Sector Conduct Authority, in respect of governance, reporting, respective responsibilities, and cooperation and coordination

The FSR Act and the revised ombud system



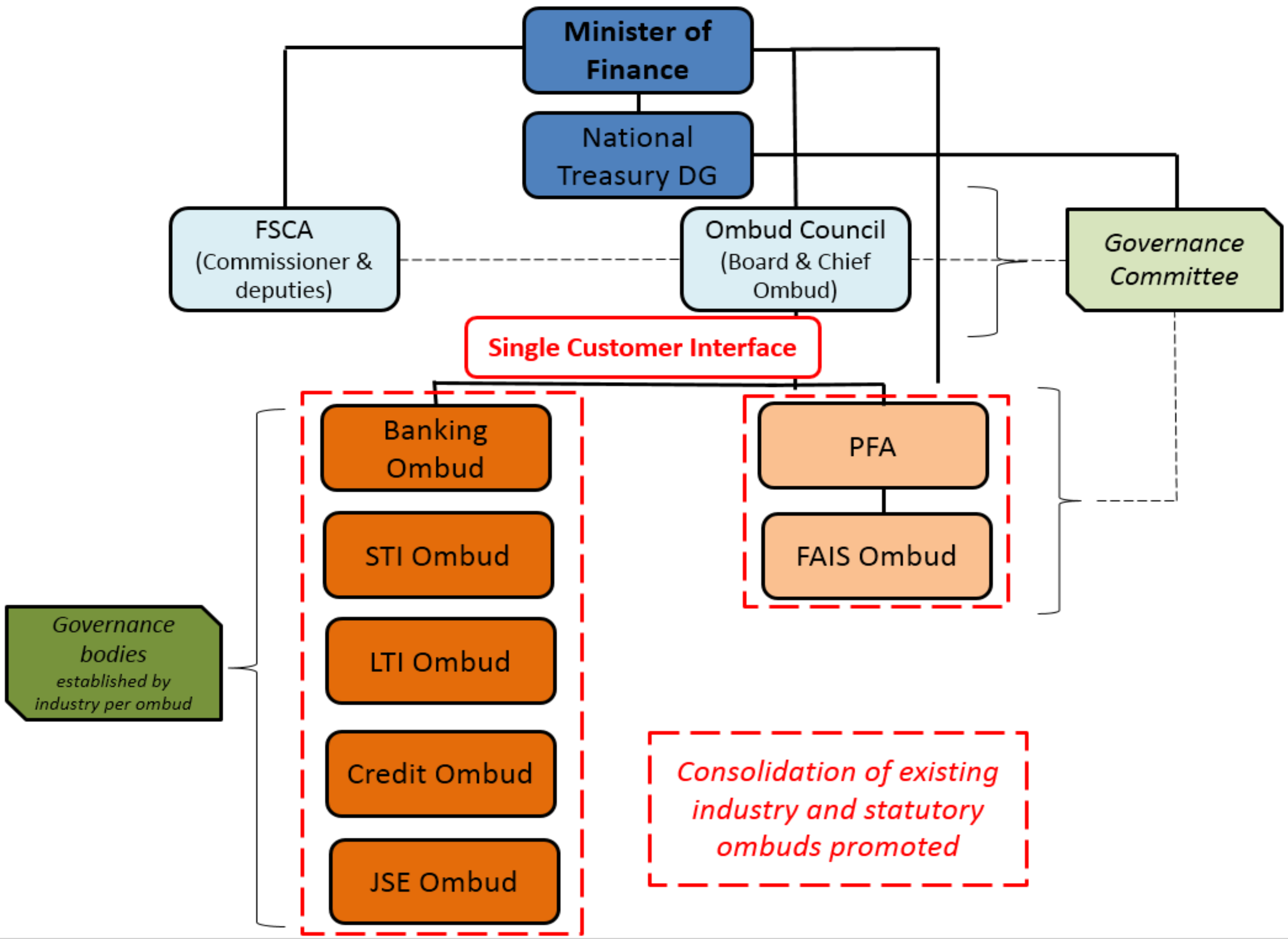
Considerations for further structural reform

- Harmonising the operation of the ombuds system is important but may not comprehensively deal with all the challenges identified. Considerations include:
  - Continued **overlap or underlap** in ombud scheme operations
  - The development of **new types of financial products and services**
  - Alignment with **continued regulatory reforms (COFI Bill)**
  - **Funding considerations** given that membership to a scheme is mandatory
  - Trends toward **increasing convergence of financial ombuds schemes**, making it simpler for financial customers to navigate dispute resolution

- In seeking to address some of these challenges, three possible models are identified for the final structure of the ombud system **(a fourth option would be to retain the current structure)**.

- The current positioning of the FSR Act **accommodates a move to each of these models**, and can therefore be seen as a stepping stone towards supporting further engagement on the preferred model for South Africa.

Model 1: A hybrid model



Model 1: A hybrid model

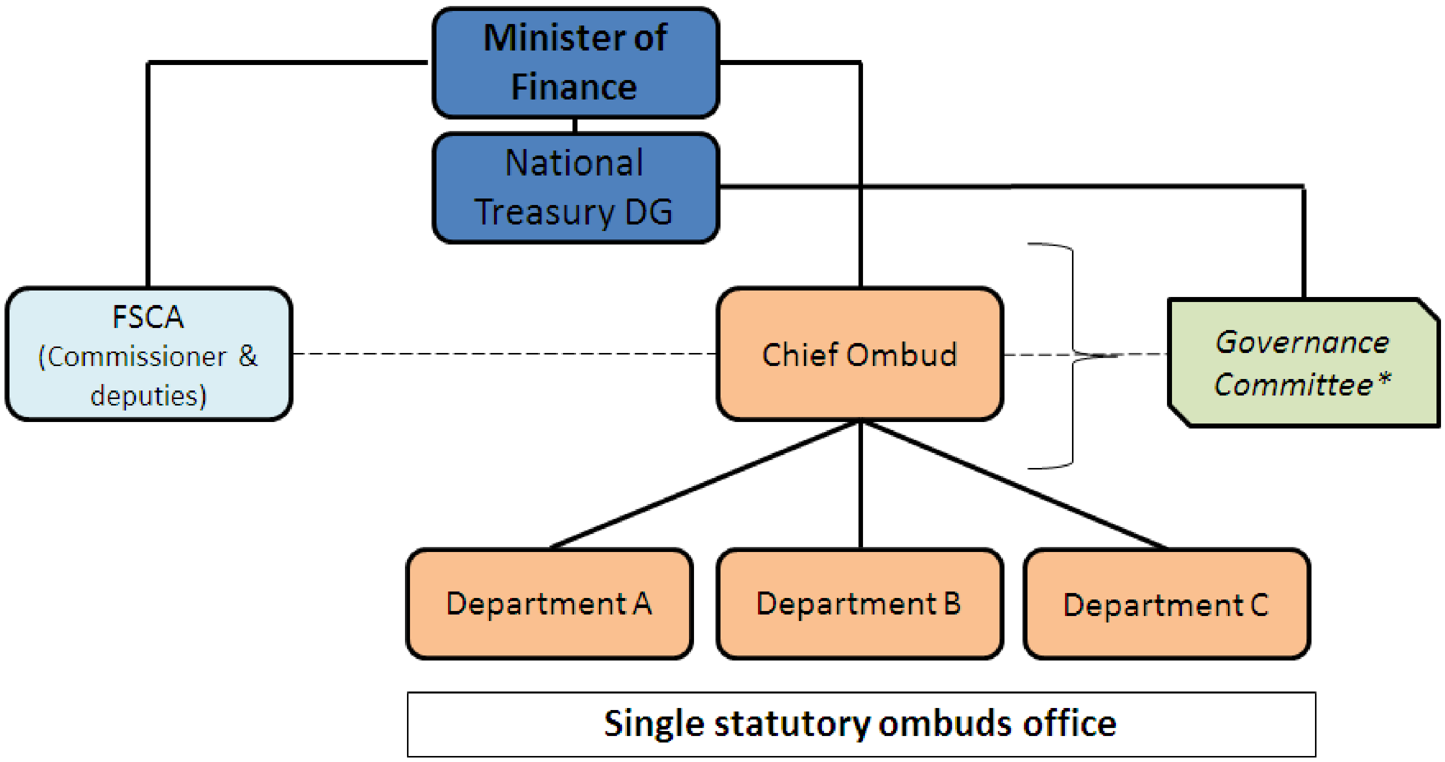
- **The Ombud Council oversees both industry ombuds and the statutory ombuds, consolidation amongst schemes promoted**

- **Main benefits:**
  - Least disruption to the ombud system, enhances status quo.

- **Main risks:**
  - Only partly addresses challenges relating to fragmentation.
  - No clear policy reason why certain types of financial activities/ entities should be subject to a statutory dispensation and not others.

- **Transition steps:**
  - Encourage consolidation of industry ombuds, investigation into and establishment of central single customer interface that will not add unnecessary delays to complaints resolution

Model 2: Centralised model, establishing a single statutory ombud scheme



** DG may appoint one governance committee to serve as the oversight body for both FSCA and Chief Ombud*

Model 2: Centralised model, establishing a single statutory ombud scheme

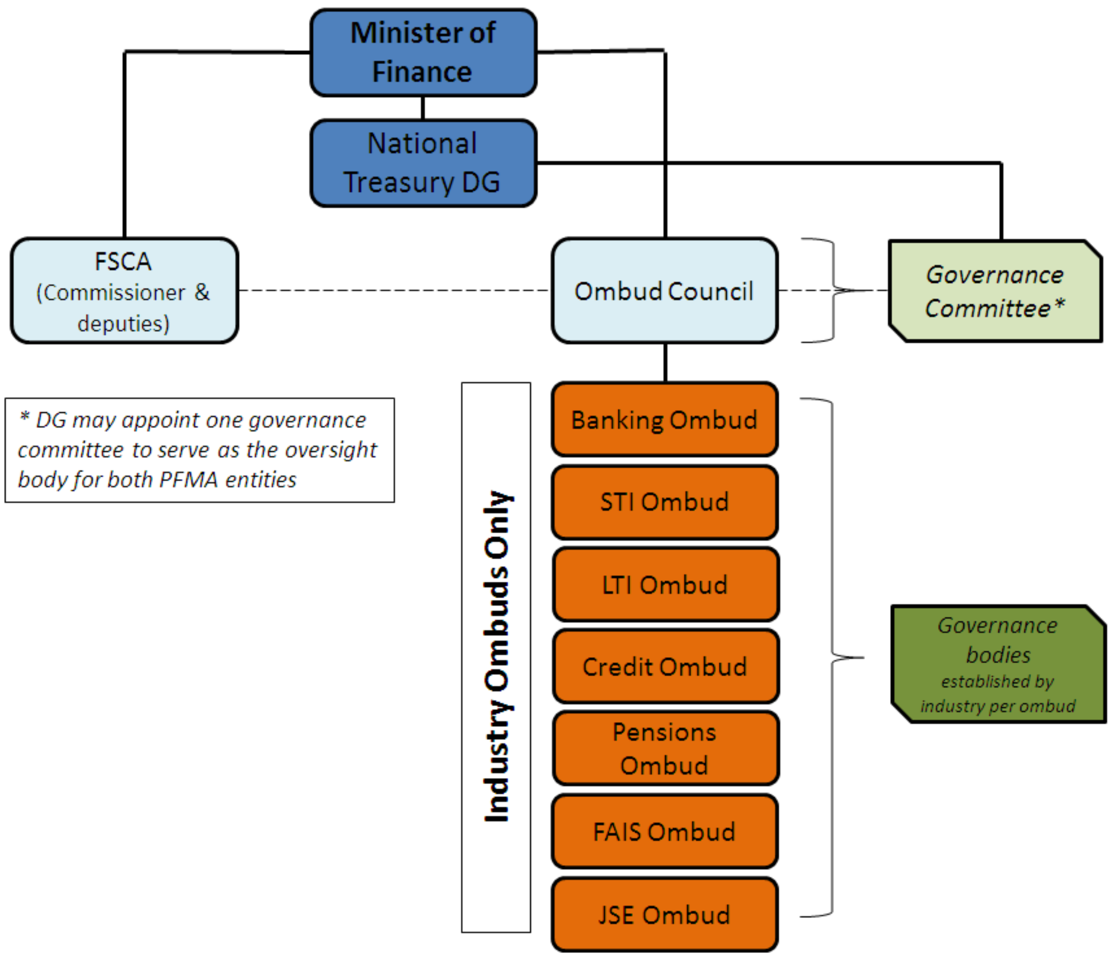
- **Single statutory ombud scheme established by law with jurisdiction over all complaints in the financial sector with different department to handle complaints.**

- **Main benefits:**
  - Simplified structure
  - Single interface for entire value chain of product provision and distribution
  - Simpler for consumers to understand
  - Full sector coverage
  - Transparent performance oversight by Minister and Parliament

- **Main risks:**
  - Expensive to set up
  - Disruptive to ombud system as it dissolves existing industry ombuds
  - May be confusing to financial customers

- **Transition steps:**
  - Operational establishment of the single statutory ombud scheme with the necessary systems and expertise, including absorbing the existing statutory schemes and dissolving stand-alone industry ombuds.

Model 3: Industry ombuds with strong oversight by the Ombud Council



** DG may appoint one governance committee to serve as the oversight body for both PFMA entities*

Model 3: Industry ombuds with strong oversight by the Ombud Council

- All financial institutions that serve the retail market are **obligated to belong to an ombud scheme**, either as a direct statutory obligation or as a condition of licensing. Such schemes are **established through industry initiative**. All schemes **must be recognised** by the Ombud Council, and are subject to oversight by the Council, including minimum standards for resolving disputes.

- **Main benefits:**
  - Cost efficient and flexible

- **Main risks:**
  - Member interference in the decision-making by the ombud
  - Disruption to ombud system as the statutory ombuds are dissolved
  - May add to the challenge of fragmentation
  - Providers of "new" types of financial products or services may struggle to identify a suitable ombud scheme.

- **Transition steps:**
  - Ombud Council remains as regulator of the ombud schemes, and the statutory ombuds are dissolved.

Way forward

- The Ombud Council is anticipated to be established alongside the Prudential Authority and Financial Sector Conduct Authority in 2018, and provisions relating to the ombuds system implemented thereafter.

- Further steps identified:

  1. An **updated review of the overall functioning and outputs of the ombud system is needed**, looking to identify performance indicators and test each ombud and the system against these. A **diagnostic into the functioning of South Africa's ombuds system will be undertaken in 2018**.

  2. **Best-of-breed standards for all ombud schemes should be proposed**, as part of the new Ombud Council's work programme. These requirements will be issued as Ombud Rules by the Ombud Council. The Council should **consider the processes and procedures that should be standardised, like complaints and referral practices, investigation powers, feedback times and methods, adjudication approaches, reporting, as well as the appropriate balance between principles-based and rules-based standards. The findings of the diagnostic will be important in this regard**

  3. In **3-5 years a review of the impact of interventions should assess whether further corrective action is necessary, including through structural reform** (as per the options contemplated in Chapter 6).

Thank you

national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA