

# Financial services need to wake up to fact that treating customers well is good business

By [Andrew Schmulow](#)

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South Africa's regulatory regime for the financial services sector is going through major changes. The question is whether companies can adapt to a principles-based approach. Or will they default back to rules-based compliance during the implementation of the [Conduct of Financial Institutions Act](#)? The aim of the new law is to improve financial sector conduct and ensure fairer outcomes, particularly for customers.



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There are strong arguments that a business that prioritises the values of good [conduct](#) will be rewarded with loyal [customers](#). They, in turn, have a high degree of trust in the business, and are more likely to source products and services from it. There are also indications that more loyal customers are less concerned about marginal differences in the price of a product or service, when compared to those of [competitors](#).

In a wider social context, the South African government has made it clear that it expects financial services companies to take seriously the idea of a [social contract](#). And that this, is essentially, their licence to operate in the financial industry.

From the industry's perspective this means that treating customers well and pursuing greater financial inclusion are a [legal requirement](#), as well as necessary to mitigate risk.

These developments reflect changed and changing expectations by wider society of the [role](#) financial service providers should play in contributing to South Africa's future.

For all these reasons, compliance with new conduct standards should be regarded as an opportunity to embed [resilience](#).

## Benefits

But these kinds of changes are often met with anxiety. Rules-based compliance is straightforward. Principles-based systems are less clear.

In my view anxiety is unnecessary, as compliance with new conduct standards serves a practical purpose.

If done in conjunction with deep reflection, compliance will steer the business towards better conduct. Moreover, a principles-based approach allows for flexibility by eschewing a tick-a-box mentality, which leaves the firm at [risk](#). In some entities, good conduct already runs deep in the organisation. What will change, even for them, is the introduction of a more structured framework, more finely targeted, and set against ideational principles, not prescriptive rules.

Put simply, the new conduct regime produces an unexpected additional benefit: through compliance with the principles of good conduct and the assurance of good consumer outcomes, firms may expect to gain greater resilience.

## **Achieving authenticity**

In practical terms, compliance that is founded in ethics and integrity brings authenticity.

To achieve this, three issues should be addressed.

The role and perception of compliance: It is important that businesses understand that compliance is not the “business prevention department” but the “business sustainability department”. Put simply, compliance should be regarded as a protector of the business and its place in society. An excellent compliance department, operating in a principles-based regime, is the vector by which the business transmits good outcomes for customers in future.

Implementation: By structuring the business around core principles, the entire organisation is brought along, and helps strengthen the underlying sub-set of narrow compliance. For this process, the compliance department must deploy a framework across the business, under the rubric that it is everyone’s job to act ethically. This envisages leveraging the existing skills, and especially in the case of highly compliant firms, long-standing expertise that is embedded within compliance.

Conduct review: Interrogating the life cycle of a product or service starts with product or service conception. This is more extensive than the customer journey. By spending time with stakeholders – including customers – to help understand why a product or service process works or does not work, these enquiries deliver significant understanding to the firm, and will deliver monetary benefits. Put differently, product performance information intelligible only to a highly educated customer will not be adequate for customers who are low income. Therefore, it would fail to comport with the underlying [principles](#) of constructing a financial system that is aimed at “protecting financial customers, promotes their fair treatment and protection, and promotes financial inclusion and the transformation of the financial sector”.

Interrogation of those processes would involve chunking conduct standards into a set of qualitative and conceptual (as opposed to analytical) enquiries. By aligning with overall corporate values, these enquiries reinforce the “all together” concept. What is also required is independence in the design of recursive reviews that will make a valuable contribution in mitigating otherwise unavoidable “observer biases”. Evidence of the problems caused by such cognitive biases are to be found in Australia, in the recent review by the Prudential Regulator of Commonwealth Bank and the Westpac self-assessment. Both allude to governance and conduct failures precipitated by a process-driven, as opposed to goal-

orientated, myopia.

## **Future-focused firms will lead the way**

Forward-thinking firms will be first movers towards stakeholder (as opposed to shareholder) [primacy](#).

This approach was recently promoted by the Australian Royal Commission as the way forward for Australian banks and insurers. The South African authorities are paying careful attention to the commission's findings.

In time, therefore, first movers in this space will no longer seem radical, but simply [early](#). Those firms will provide the definition of leadership in the industry. If being values-driven is an end in itself, then first movers will enjoy an advantage. Moreover, credibility in this space affords firms the opportunity to set the standards to which the regulator will hold the rest of the industry.

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