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Financial Services Authority

Treating customers fairly: progress update

June 2008

We would welcome any comments on issues raised in this document. You can send us comments by e-mail: tcf@fsa.gov.uk.

Alternatively please send your views in writing to the following address:

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It is the FSA's policy to make all responses available for public inspection unless the respondent requests otherwise.

Copies of this document are available to download from our website – www.fsa.gov.uk.

Contents

Audience

We strongly encourage all firms with business relevant to the retail market to read this publication. The Executive Summary is particularly relevant to CEOs and senior management and includes our key messages.

The Annexes provide examples of good MI measures which senior management in firms of all sizes may wish to consider applying to their business.

1 Executive summary

Update on TCF progress by March 2008

- This paper reports on the progress that firms have made against the March interim deadline, by which point they should have had appropriate management information (MI) or measures in place to test whether they are treating their customers fairly.
- The March deadline was set as an interim deadline to encourage firms to focus on and make progress with demonstrating improved outcomes for retail consumers. Our assessment of firms focused on their *ability* to *measure* outcomes, as a precursor to the final deadline in December, when they will be expected to demonstrate that they are consistently treating their customers fairly.
- Firms should not have to produce large volumes of MI, nor MI specifically labelled TCF MI or mapped directly to the TCF Outcomes. They should understand how it relates to the TCF Outcomes but may not necessarily label it in this way for business use. Thoughtful evidence and proper analysis will enable a firm to identify, measure and manage the quality of outcome it delivers to consumers, and so to ensure that it is consistently fair.
- Whilst only a minority (13%) of the sample of relationship-managed firms we assessed met the deadline on time, we believe that with a very substantial, continuing effort approximately 80% of the sample are still capable of meeting the December deadline.
- Of the relationship-managed firms that failed to meet the deadline on time, we saw a very broad spectrum of results: from those firms that had invested significant time and energy and so almost met the deadline, right through to firms we have considered for investigation and enforcement action on grounds of potential or actual consumer detriment. All firms that failed to meet the deadline on time have received a strong message that urgent progress is needed.
- We have used a range of other regulatory tools, including in some cases requesting an audience with the firm's Board, requiring the firm to commission help from auditors or consultants ('skilled persons') or encouraging firms to seek such external assistance.

- In January 2008, we launched our small firms enhanced strategy with the aim of further helping small firms to achieve and demonstrate the TCF Outcomes. It is too early in the life of the enhanced strategy for us to have tested the methodology sufficiently or to have assessed a representative sample and we are not therefore reporting on small firms' progress at this stage. Results of the enhanced strategy will not be published before the end of Q4 2008. In the meantime we have included some further case study material which we believe will help small firms make further progress.

Next steps for firms

- We expect all firms to undertake a significant amount of further work with a great deal of energy to ensure they meet the December 2008 deadline, to demonstrate that they are consistently treating their customers fairly.
- To help firms further, we have included examples of good and poor practice in this progress update. We strongly encourage firms to consider the examples in the context of their own business model.
- To meet the December deadline firms will have to:
  - demonstrate that senior management have instilled a culture within the firm whereby they understand what the fair treatment of customers means; where they expect their staff to achieve this at all times; and where (a relatively small number of) errors are promptly found by firms, put right and learned from;
  - be appropriately and accurately measuring performance against all customer fairness issues materially relevant to their business, and be acting on the results;
  - be demonstrating through those measures that they are delivering fair outcomes; and
  - have no serious failings – whether seen through MI or known to us directly – including in areas of particular regulatory interest previously publicised by the FSA.

Next steps for the FSA

- In order to help firms make sufficient progress towards December and to be able to assess performance against that deadline, we will:
  - use every opportunity – including those presented by ongoing engagement with individual firms via ARROW visits and through the existing programme of thematic work – to remind firms what is required;

- continue to take tough action on the worst firms by focusing on and dealing more visibly and forcibly with a targeted group of those firms who are failing to deliver fair treatment of customers. This may include relationship-managed firms that failed to meet the March deadline, those firms who are failing to deliver TCF as identified through ongoing ARROW assessments, and firms identified by other indicators such as results of thematic work; and
- undertake assessments between January and June 2009 using a sample of relationship-managed firms (which will be structured to include firms from relevant sectors). We will use the results of these assessments along with other evidence on outcomes available to us at that time, to assess industry progress. We will continue to monitor the progress of small firms via the enhanced strategy.

- We currently expect to publish the results against the December deadline in September 2009.
- Thereafter, the FSA will cease to have a bespoke 'TCF initiative'. Instead, the assessment of how firms treat their customers will become a part of business-as-usual. Through ARROW reviews (in the case of relationship-managed firms), the enhanced strategy for small firms, and thematic work (for all) we will both review firms' own MI or evidence of how they treat their customers and test outcomes directly ourselves. This will therefore build on the approaches developed over the past few years.

2 Background

Purpose of the paper

1. The purpose of this paper is to:

- report on the progress that firms have made against the March interim deadline, by which point firms should have had appropriate management information (MI) or measures in place to test whether they are treating their customers fairly;
- focus firms' attention urgently on meeting the final deadline for TCF – by the end of December 2008 firms should be able to demonstrate that they are consistently treating their customers fairly. This requires having appropriate MI in place, using it and addressing any shortfalls so that by December the firm is consistently treating customers fairly. We recognise that many firms have found identifying, collecting, and using MI for TCF challenging so we have included some examples of good and poor practice to support firms in meeting their TCF requirements; and
- explain both how the FSA will take forward its work on TCF in the next phase and how assessment of fair outcomes will be carried forward into business-as-usual in the future.

The 2008 deadlines

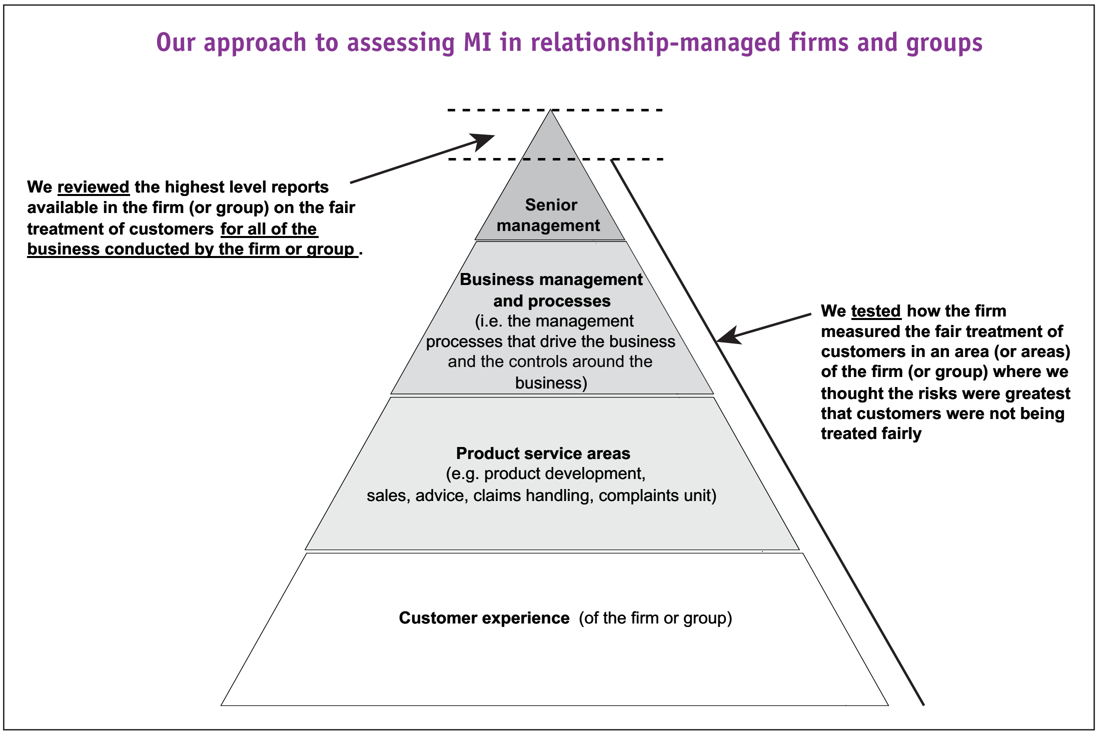
2. We set two important TCF deadlines for firms this year. By the end of December 2008, firms are expected to be able to demonstrate they are consistently treating their customers fairly (ie their MI or other measures should show good results). One way for firms to do this is to provide evidence to demonstrate they are meeting those TCF Outcomes that are relevant to their business. Evidence that the firm is treating customers fairly will vary with the size and complexity of the firm.

3. To encourage firms to focus on this area, we set an interim deadline that by March 2008, firms were expected to have appropriate management information or measures in place to test whether they were treating their customers fairly (ie to be able to measure outcomes). This reflects Principle 3 of our Principles for Businesses that 'a firm must take reasonable care to organise and control its affairs responsibly

and effectively, with adequate risk management systems', as well as the specific SYSC requirement that 'a firm must take reasonable care to establish and maintain such systems and controls as are appropriate to its business'[1].

How we measured progress

Relationship-managed firms



4. Most large retail groups and a sample of all other relationship-managed firms with business relevant to the retail market have been assessed against the March deadline. We assessed 96 relationship-managed firms in total.

5. To do this we undertook detailed assessments of firms' MI with the aim of addressing three points:

- The adequacy of the measures – do they actually capture the outcome in question?
- The integrity of the measures – where a firm says it is measuring the suitability of advice for example, is it doing so accurately?
- The operational use of the material – firms needed to show that the material was in an operational state even though there may not yet be a track record of using it.

1 FSA Handbook, SYSC 3.1.1R. See also SYSC 3.2.11G which states that 'A firm's arrangements should be such as to furnish its governing body with the information it needs to play its part in identifying, measuring, managing and controlling risks of regulatory concern. Three factors will be the relevance, reliability and timeliness of that information.'

6. We reviewed the pre-assessment questionnaires submitted by firms outlining the measures used to capture the outcomes that were relevant to them, and how these measures were collated and reported within the firm. We then reviewed the reports used by management. To understand how the MI was derived and how it was used, we also interviewed a cross-section of staff that use and produce management information.

7. For large relationship-managed firms or groups where we did not have resources to review evidence across the entire business, we reviewed the highest level TCF reports available, covering the range of the business that the firm or group conducted. We then tested how the firm measured the fair treatment of customers in a key area (or areas) of the firm (or group) where we thought there was the greatest risk that customers were not being treated fairly.

8. These assessments were subject to extensive moderation. For more information on the assessment process, see Annex 1.

Small firms

9. The March and December TCF deadlines apply to both large and small firms. However, in line with our enhanced strategy we have used a different methodology to assess smaller firms. For more information on the small firms enhanced strategy, see Annex 1.

10. Work to date does not give a representative sample from which conclusions can be drawn and moreover we are still testing the methodology. Results for small firms will not be published before the end of Q4 2008.

11. Nevertheless, early signs are encouraging. We are seeing much greater awareness and engagement on TCF from small firms than hitherto – and, as we have seen before, once small firms are engaged they can make quick progress on TCF.

12. Our methodology has enabled us to identify some early lessons for smaller firms, including on MI and therefore we have included some small firms case study material as Annex 2A. Further help for smaller firms on TCF is available on our website which we will continue to update as the enhanced strategy progresses.

Examples of good and poor practice

13. We previously produced a range of materials on MI that may be useful for firms including a so-called 'cluster report'[2] containing a good and poor practice, a guide to management information[3] and real examples from our work with firms on measuring progress against the six TCF Outcomes[4]. In our February update[5] we also listed common themes we had seen in assessment of firms to date.

2 'Management information cluster report', July 2006
3 'Treating customers fairly – a guide to management information', July 2007
4 See our TCF webpages at http://www.fsa.gov.uk/Pages/Doing/Regulated/tcf/management/index.shtml
5 'Meeting the 2008 deadlines', February 2008, see our TCF webpages at http://www.fsa.gov.uk/Pages/Doing/Regulated/tcf/progress/index.shtml

14. Now that firms have done extensive work on MI, we are able to provide further material in the form of actual good and poor practice examples we have seen in relationship-managed firms. This is provided at Annex 2B of this paper. In compiling these examples, we relied extensively on the information provided to us by firms themselves, either in interviews, or through MI packs.

15. Many of the trade associations have produced helpful material on TCF. Some have also amplified on our material on MI for their members.

16. While we have given examples of good practice, they are not minimum standards nor do they amount to guidance under the Financial Services and Markets Act (FSMA).

3 Progress against the March interim deadline

Relationship-managed firms

17. Whilst only a minority (13%) of the sample of relationship-managed firms we assessed met the deadline on time, we believe that with a very substantial, continuing effort approximately 80% of the sample are still capable of meeting the December deadline.

18. Of the relationship-managed firms that failed to meet the deadline on time, we saw a very broad spectrum of results: from those firms that had invested significant time and energy and so almost met the deadline, right through to firms we have considered for investigation and enforcement action on grounds of potential or actual consumer detriment. All firms that failed to meet the deadline on time have received a strong message that urgent progress is needed.

A firm that almost met the March deadline

This firm had a good set of MI which was 'owned' by senior management. The MI was well constructed and easy to interpret and use. The use of MI was integrated into the existing governance structure, and the firm was able to point to real examples of where the MI was being used by management to understand the quality of outcomes being delivered to its customers and tackle identified issues. The reason the firm did not meet the deadline was because as at the end of March 2008 there were still some gaps in the MI – areas where the firm was not yet measuring whether they were meeting all the TCF Outcomes relevant to the firm. The firm was working to tackle these gaps and is in a strong position to meet the December deadline.

A firm that failed to meet the March deadline

This firm was significantly behind where they should have been by the end of March, partly because they had shown little urgency in tackling what they had to do to meet the deadline. The firm's staff were unable to articulate the key areas where they needed to identify, measure and manage the quality of consumer outcomes. Furthermore, what measures the firm did use were weak – they confused satisfaction with fairness and senior management were not effectively overseeing the use of MI across the firm.

General trends

19. We have not identified any significant sector-specific variations. However, we have seen general trends that distinguished firms that met the deadline from those that did not.

20. We have analysed the findings from our assessments and have highlighted some common themes for those that met the deadline and those that failed to do so.

Characteristics of firms that met the deadline

Many firms that passed the March deadline had positive cultural indicators regarding TCF.

Firms' own commercial strategies were consistent with fair treatment of customers

Those firms which had built fair treatment of customers into their commercial strategy, or which had made the effort to articulate how they could map the TCF Outcomes to their strategy, found it easier to measure fair treatment. However, firms who simply claimed that they always put customers first often assumed they were treating customers fairly, but could not always demonstrate how they knew this. Without MI, these firms were not in a position to identify where they might not be treating their customers fairly.

Firms demonstrated active senior management involvement

The role of senior management, and the information they see – or do not see – can be critical. On the whole, where senior managers played an active, directive role in setting out what the firm needed to do to embed fair treatment in the firm's operations, the firm developed a more realistic and effective measurement of it.

Firms ensured that the fair treatment of customers was written into personal objectives and reward at all levels within the company

Some firms referred to fairness in objectives without being clear on how they would assess and measure delivery of fair treatment. Those firms who clearly articulated how delivering fairness influenced bonus payments performed best against the March deadline. In some cases, firms combined this approach with strong and effective internal staff forums and TCF training. They then linked this to the firm's overall approach to performance management and reward, taking into account how fairness related to individual roles.

Firms listened to, and acted on, feedback from customers

Firms that took customer feedback seriously, including senior management exposure to such feedback, were more likely to meet the March deadline. Firms have found it particularly difficult to test the clarity of their information to consumers. As well as reacting effectively to queries and complaints, some firms that met the March deadline adopted a number of creative approaches to this, such as establishing regular customer feedback forums to check ease of understanding and to assess requirements. Not only did this allow firms to check for understanding of existing and new products, it also enabled firms to anticipate customer views rather than just react after poor consumer outcomes had occurred.

Characteristics of firms that failed to meet the deadline on time

Firms failed to give TCF enough effective sponsorship at the most senior levels

Particularly in more complex firms, where there are a number of distinct operating units, or a legacy of different cultures due to previous absorptions of other firms, it was important to have active endorsement and support at the most senior levels in order to be able to provide momentum and to drive though necessary actions in order to meet the March deadline on time. Firms that delegated this task to a project manager or to compliance, or where the senior management team showed no active involvement or interest in the progress of this work, failed to achieve the necessary progress.

Firms placed too much reliance on existing business-as-usual MI

Effective MI to measure fair treatment needs a clear, thoughtful analysis of whether fair outcomes are being delivered for consumers and requires appropriate measures to monitor them. This may well include existing or business-as-usual MI but may also require other measures or that business-as-usual measures are considered differently and from a TCF perspective. In many cases, simply reporting operational MI ('bottom-up') as 'TCF reports' led to senior management being swamped with too much detail and with no clarity on the important fairness issues. Lots of operational MI produced vast amounts of readily available material. However, it did not provide an effective view and lacked commentary and analysis or actions on how the firm was addressing any issues.

Firms underestimated the scale of the challenge and started too late

Many firms did not really understand what was required until they started to prepare their own MI. When they did so it became apparent that they had to think about what they had to measure, the MI they might need and the nature of analysis and reporting upwards that would be effective. A large number of the firms who failed to meet the deadline on time may have succeeded if they had started earlier.

Firms confused process with outcomes

MI to demonstrate fair treatment should generally focus on how far a firm is delivering fair outcomes rather than measuring processes. Information on process can be helpful but process measures are not enough to demonstrate delivery of TCF Outcomes without other supporting evidence. Lots of firms measured and reported on their processes but did not give enough thought as to whether or not those processes were really measuring the fair treatment of customers. For example, some firms measured whether complaints had been answered promptly. This can be a useful indicator of the service being provided however this measure alone does not demonstrate that the outcome for the customer is fair. Another example is that some firms measured the number of annual product reviews carried out but did not provide sufficient insights on how the results of the reviews demonstrated whether consumer outcomes delivered by the products were likely to be fair. Firms should ensure that any such reviews give proper consideration to fair customer treatment. Issues arising should be communicated to appropriate management and appropriate action should be taken.

Firms confused satisfaction with fairness

Lots of firms took great pride in being able to point to high levels of customer satisfaction and emphasised their customer service ethos. However, many customer satisfaction surveys were inadequate evidence of fair outcomes for three reasons:

- Many such surveys were reported as one aggregated result when many of the underlying questions being asked were nothing to do with fairness. For example, 'was the branch clean when you walked in?'.
- Even where customer surveys were focused more on fairness, they asked questions that customers were unlikely to be able to answer effectively. For example, 'were you satisfied you had all the risks properly explained to you?'.
- Many firms failed to test the clarity of their information. For example, in some cases firms put a lot of effort into redrafting customer-focused material, and checked that it was being delivered promptly, but did not consider whether or not customers would be able to understand the material sufficiently to take appropriate action and exercise 'caveat emptor'. We do not expect firms to show that consumers have understood, but believe that they could do more to ensure their material is capable of being understood by its target audience.

What we are doing with firms that failed to meet the March deadline

21. For firms that have failed to meet the March deadline on time and where we have confidence that the firm's management will address any issues effectively, we have set out clearly our expectations of what they now need to achieve. We have also set deadlines to prioritise the firm's efforts on resolving issues as soon as possible.

22. We will monitor the progress of these firms. We will undertake similar intervention with other firms which we have not yet visited, but where we find similar issues in forthcoming ARROW or other visits.

23. Where relationship-managed firms have failed to meet the deadline on time and we think it unlikely the firm is capable of meeting the December deadline without significant regulatory intervention we have:

- reviewed each firm individually to determine whether enforcement action is merited – on grounds of potential or actual consumer detriment – and made one referral to enforcement so far. In line with the commitment set out in our Business Plan 2008/09, where we see evidence that outcomes are not improving despite clear messages to industry, we will seek to increase penalties to achieve our goals;
- requested an audience with the Boards of a number of firms to discuss the issues;
- required further action from firms' senior management, including following up remedial action plans. One firm has engaged consultants to carry out a review and in another firm we have required a Skilled Persons Report (Section 166);
- requested further information for analysis from the firm, to enable us to analyse what the underlying issues hindering fair outcomes are and determine what further regulatory action might be necessary (two cases); and
- used FSA specialist teams to carry out follow-up visits to check whether sufficient subsequent progress has been made (three cases).

CASE STUDY: Failing to take reasonable care to ensure that advice is suitable, and failing to have adequate systems and controls for the sale of Payment Protection Insurance (PPI)

In the past the FSA has taken action against a firm where:

- the firm's procedures did not require advisers in its branch network to gather sufficient information about customers' circumstances and take sufficient information into account when considering whether PPI was suitable; and
- the firm did not require advisers to explain fully why they recommended a particular policy or identify to customers any demands and needs which the policy would not meet.

These and other failings meant that the firm put its customers at an unacceptable risk of being sold PPI when it was not suitable for them.

In addition, we found that as a result of inadequate systems and controls:

- the firm did not have effective systems to train and monitor its staff and failed to ensure that its procedures for monitoring sales staff effectively identified and investigated potentially unsuitable sales;
- management information provided to senior management was not sufficient to enable them to identify problems with the sale of PPI; and
- its records were not sufficient to demonstrate its sales were suitable.

4 Meeting December's deadline

What we expect firms to do next

24. In November 2007 we reported that while senior management in firms are taking TCF seriously and building it into their culture, there was little evidence that this was translating into improved outcomes for consumers. Many firms – even some of those who have passed the interim deadline – still have much to do to demonstrate and deliver fair outcomes for consumers.

25. Our assessment of progress against the March deadline focused on whether firms have the appropriate management information or measures in place to test whether they are treating their customers fairly. As well as collecting such evidence, we will now expect all firms to use it effectively and increasingly to be able to show through it that they are consistently treating their customers fairly.

26. To meet the December deadline firms will have to:

- demonstrate that senior management have instilled a culture within the firm whereby they understand what the fair treatment of customers means; where they expect their staff to achieve this at all times; and where (a relatively small number of) errors were promptly found by firms, put right and learned from;
- be appropriately and accurately measuring performance against all customer fairness issues materially relevant to their business, and be acting on the results;
- be demonstrating through those measures that they are delivering fair outcomes; and
- have no serious failings – whether seen through MI or known to us directly – including in areas of particular regulatory interest previously publicised by the FSA.

27. There are a number of regulatory issues which we have highlighted and for which we have made our expectations clear either as thematic priorities or in the Financial Risk Outlook 2008. We would be particularly concerned about these issues if they were still evident in firms at December 2008 and we will be looking for MI to show that action has been taken and that these issues have been fixed. Similarly, we will expect that firms have tackled any major consumer protection issues previously raised by the FSA directly with the firm. To assist firms, we have included some examples of MI around known regulatory issues [see Annex 3].

What we are doing next

Ongoing engagement with firms

28. We plan to use every opportunity – including those presented by ongoing engagement with individual firms via ARROW visits and through the existing programme of thematic work – to remind firms what is required.

Risk based challenge – taking tough action on failing firms

29. We will continue to take tough action on the worst firms by focusing on and dealing more visibly and forcibly with a targeted group of those firms who are failing to deliver fair treatment of customers. This may include relationship-managed firms that failed to meet the March deadline, those firms who are failing to deliver TCF as identified through ongoing ARROW assessments, and firms identified by other indicators such as results of thematic work. Where appropriate we will publish the action we take.

Assessing a sample for establishing progress

30. We will undertake assessments between January and June 2009 using a sample of relationship-managed firms (which will be structured to include firms from relevant sectors). We will use the results of these assessments along with other evidence on outcomes available to us at that time, to assess industry progress as at December 2008.

31. We will incorporate our assessment work into ARROW. Where outside of the ARROW cycle, we will bring forward the TCF part of an ARROW assessment. We will form an evidence-based judgement on the firm's overall culture, on the quality of the information that it is using to measure its outcomes for consumers, and on what that information (and anything else we might know about the firm) tells us about what the firm is actually managing to achieve. And, as with the March deadline, to test the quality of a firm's information we will need to test outcomes at the firm directly ourselves – for example, through reviewing consumer documentation and advice files, and listening to customer calls. We will continue to monitor the progress of small firms via the enhanced strategy.

32. When we publish the results of progress against the December deadline, we will take account both of the sample of specific assessments and of other evidence on outcomes available to us at that time. This will include evidence from other FSA work and evidence from external sources. This evidence base will inform our judgement as to the degree to which fair outcomes for consumers are being achieved on a consistent basis.

33. We currently expect to publish the results against the December deadline in September 2009.

34. Thereafter, the FSA will cease to have a bespoke 'TCF initiative'. Instead, the assessment of how firms treat their customers will become a part of business-as-usual. Through ARROW reviews (in the case of relationship-managed firms), the enhanced strategy for small firms, and thematic work (for all) we will both review firms' own MI or evidence of how they treat their customers and test outcomes directly ourselves. This will therefore build on the approaches developed over the past few years.

Methodologies for assessing relationship-managed firms and small firms

Our approach to undertaking MI assessments of relationship-managed firms

We undertook detailed assessments of relationship-managed firms' MI with the aim of addressing three points:

- The adequacy of the measures – do they actually capture the outcome in question?
- The integrity of the measures – where a firm says it is measuring the suitability of advice for example, is it doing so accurately?
- The operational use of the material – firms needed to show that the material was in an operational state even though there may not yet be a track record of using it.

In our assessments we sought to establish whether the firm had robust measures against all the TCF Outcomes – which were appropriate for that firm – to enable it to test whether it was treating its customers fairly.

For large retail groups, we looked at the high-level evidence on the treatment of customers across all the firm's business and focused on how the firm measured the treatment of customers in areas of the firm's business where the risks to the fair treatment of customers were higher.

Assessments were made up of three stages:

- collecting the information we needed to help focus the assessment;
- undertaking the assessment and drawing up our conclusions; and
- ensuring our conclusions were consistent with other assessments and feeding back the results of the assessment to the firm.

Our assessments took place at the same time as ARROW risk assessments or, where this was not possible, we carried out a separate assessment. Assessments were undertaken by the firm's relationship manager with assistance as necessary from a central TCF resource.

How we undertook assessments and the information we requested from firms

Most firms completed pre-assessment questionnaires which outlined the management information and other measures used by the firm to evidence the fair treatment of customers. We also reviewed copies of reports used by senior management to demonstrate to themselves that the firm treats its customers fairly. Based on this information and anything else we already knew about the firm, we determined which areas to focus on as part of the assessment.

To understand the source of the MI, how it was used and the actions that were taken as a result of its review, we spoke to staff that use and produce management information, and we also interviewed senior management about the reports they receive on the fair treatment of customers across the firm. We often tested the customers' experience of the firm to assess whether the management information picked up the key TCF issues in the firm. For example, this included sampling calls made by customers to the firm, or reviewing a small number of customer files.

How we have ensured a consistent approach including giving feedback to firms

All assessments have been through a moderation process involving FSA staff with TCF expertise and representatives from the Division responsible for the supervision of the firm. A sample of assessments has also been subject to cross-FSA moderation.

Our approach to assessing the progress of small firms

In January this year we announced that we would be increasing our supervision of and contact with small firms, aiming to further help them to achieve the TCF Outcomes. Since then we have embarked on a three-year regional programme to assess how the management of small firms approach TCF and embed it into their business. Even though the assessments will continue after the December 2008 deadline, we are seeing signs that the increased contact with small firms and dedicated TCF communications are already having a positive impact.

The assessment is based on the small firm management behaviours framework[6] as it is only through establishing and maintaining the right behaviours that management of small firms can ensure that their good intentions actually result in good outcomes for consumers. The assessment looks at the relationship the firm's management has with its staff, how it communicates TCF to its entire staff (not just advisers), and what controls, including management information, it has in place to demonstrate consistent fair treatment of customers.

6 In 'Treating customers fairly – culture', July 2007, we published a 'management behaviour framework' for small firms.

In our communications with small firms, we are continuing to emphasise the importance of their embracing TCF and the support that is available for firms that engage with us. At the same time, we will continue to take a tough approach with those firms who choose not to raise their standards, including where appropriate use of enforcement action.

To explain the assessment process and our expectations regarding TCF to small firms we have introduced new, interactive roadshows linked to the regional assessment programme. Firms are able to find out more about how to meet their TCF obligations, work through real TCF issues that may affect their firm, and learn from other firms about how they approach TCF. We are also continuing to make use of case studies/examples of good and bad practice to illustrate the various ways in which they can meet their TCF obligations. See Annex 2A for small firms case study material.

Small firms case study material

Our enhanced strategy has enabled us to identify some early lessons for smaller firms, including on MI and therefore we have included some small firms case study material here. We hope this material is useful for smaller firms to build on, to develop suitable MI for their business. Further help for smaller firms on TCF is available via our website and we will continue to update this as the enhanced strategy progresses.

The examples of good practice in Annexes 2 and 3 are illustrative. They are not minimum standards nor do they amount to guidance under the Financial Services and Markets Act (FSMA).

The examples do not seek to be comprehensive ie the firms may well need other measures not detailed here to demonstrate an outcome or have other measures that are more appropriate to their business.

We do not expect firms to use all of the measures we have provided, nor do we expect firms to highlight their mapping to the specific TCF Outcomes within that MI. Firms may however be expected to explain to an FSA supervisor how their MI maps to TCF Outcomes, in order that the firm and supervisor can understand coverage. MI or other measures should be appropriate to the size and complexity of the business and cost effective.

TCF should not generally require the creation of substantial amounts of new information. In many cases firms may analyse existing MI to demonstrate fair treatment by considering "what is the MI telling the firm about how they treat their customers?"

Although the TCF Management Information Matrix on page 5 of this Annex includes examples taken from firms achieving good outcomes with the help of compliance consultants, we have also seen examples where good outcomes have been achieved without their services. We do not require firms to seek professional advice on how to embed TCF in their business.

We have also noted that some firms have found customer feedback questionnaires to be helpful. We have observed that these only provide useful information on whether TCF outcomes are being achieved where they go beyond requesting feedback on customer satisfaction and gather information on actual customer understanding of products, services and risks.

Case Study 1

General Insurance Broker – good practice example

TCF Culture (Management behaviours)

The firm demonstrates good performance and commitment to TCF on all the drivers. Measures include:

Leadership

- Appropriate manager/principal appointed 'TCF Champion' with overall responsibility for delivering on the TCF Outcomes.

Business decisions

- Firm has strongly engaged with TCF by using both internal and external resource to formulate a TCF Strategy and Action Plan; this is a living document and regularly reviewed.

Recruitment training and competence

- The approach to recruitment and training focuses on delivery of TCF outcomes.

Controls

- Firm regularly reviews the panel of insurers used to ensure access to markets that meet customers' needs and demands.
- Marketing material is reviewed by external consultants to ensure it meets TCF requirements and appropriate senior management sign off procedures are in place.
- Complaints are regularly reviewed at senior management level and root-cause analysis findings are acted on.

Reward

- The firm has targeted reward structures in place, however advisers' performance against these are closely monitored to ensure any conflicts of interest that arise are effectively managed. For example top performers are subject to increased file reviews to double check suitability and advisers are not rewarded on business that fails to pass these checks.
- Good TCF behaviours and ideas are recognised and rewarded.

Case Study 2

Financial Adviser – good practice example

TCF Culture (Management behaviours)

The firm demonstrates good performance and commitment to TCF on all the drivers. Measures include:

Leadership

- Firm acknowledges that responsibility for ensuring delivery on TCF throughout the business rests solely with them.
- Firm worked with a compliance consultant to build a TCF strategy for the firm, and to help develop processes and procedures to deliver good outcomes for consumers as well as measures to test that they are working.

Business decisions

- Firm conducted a gap analysis and asked staff to provide ideas and as a result improved several areas of its business to ensure consumers were treated fairly.

Controls

- Firm proactively monitors completeness and suitability of advice provided using risk based criteria. High risk business and business produced by inexperienced advisers were subject to increased scrutiny.
- Firm regularly reviews a range of key performance indicators for advisers including business spread, cancellations, not taken up rates, execution only and complaints.
- Firm evidences that where the management identified an adverse trend with an adviser, appropriate action was taken to contact and review the clients at risk. Additional support and monitoring for the adviser was provided.
- Firm continually monitors information on product providers and provided examples of not using particular providers due to poor customer service and claims ratios.

Recruitment, training and competence

- Firm advisers regularly observed with clients by senior management and formal feedback provided.
- Firm advisers' ongoing professional development activities are monitored and encouraged.

Reward

- Uses a customer agreed remuneration approach and when taking trail commission offers regular reviews for clients.
- Advisers' remuneration packages include an incentive for meeting TCF related Key Performance Indicators (KPIs).

Case Study 3

Mortgage broker – good practice example

TCF Culture (Management Behaviours)

The firm demonstrates good performance and commitment to TCF on all the drivers. Measures include:

Leadership

- Gap analysis/business review is owned and driven by senior management.
- Staff feedback is collected through staff surveys to help all staff understand and embrace TCF culture and ethos of the firm.

Business decisions

- Customer feedback measures fairness, not just a gauge for satisfaction.
- Customer complaints are used to improve customer service and also to identify staff training requirements and review processes and procedures.

Controls

- Monitoring in place to ensure fact finds are fully completed, including affordability, attitude to risk and demands and needs, to enable advisers to make appropriate and suitable recommendation.
- Firm uses external consultant to provide independent review on sales process and the quality of advice.
- Firm uses file monitoring to compile trends on advisers.

Recruitment, training and competence

- Firm has formal recruitment process which incorporates TCF through knowledge tests and case studies.

Reward

- The bonus policy incorporates TCF through measuring qualitative standards relating to file reviews and complaints.

Further good practice examples for small firms

The TCF Management Information Matrix below sets out further examples of MI that small firms are collecting and using to measure their performance against the relevant TCF Outcomes.

This information is drawn together regularly and reviewed by managers/principals, and acted upon where it indicates potential risks to the TCF Outcomes being achieved.

TCF Management Information Matrix

TCF Outcome	Types of MI	Measurement
1. Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.	• TCF Self assessment/Gap Analysis and action plan. • Compliance consultants reports. • Results from internal surveys seeking staff input on TCF strategy. • Training & Competence reports. • Reports on staff performance against relevant TCF related measures (for example, KPIs regarding areas such as complaints received, cancellations, lapses, not taken up rates etc). • Reports on products sold (by type/provider). • Review of Service Standards.	• Senior management progress and commitment to embedding TCF throughout the business. • Progress on Implementation of Compliance Consultant recommendations (where received), or action following own review. • Staff engagement with TCF. • Senior management's success in communicating TCF throughout the business. • High pass rates when staff assessed for competence. • Staff demonstrate a good knowledge of TCF and TCF risks and adherence to internal policies to achieve TCF. • Identification and effective management of conflicts of interest. • TCF not impaired by poor customer handling.
2. Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.	• Customer feedback questionnaires. • Results from selective sampling of execution only business.	• Customers demonstrate a high level of understanding of marketing materials, in particular relating to products, services and risks and not just satisfaction. • Customers recorded as execution only genuinely did not require or receive advice.
3. Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.	• Results of file monitoring including records of information obtained from and provided to the customer. • Mystery Shopping Reviews. • Observed customer interviews. • Customer feedback questionnaires.	• High level of clarity and accuracy of written and oral communications with customers. • Information provided in an appropriately timely fashion. • Customer feedback demonstrates good understanding of information provided, and not just satisfaction.
4. Where consumers receive advice, the advice is suitable and takes account of their circumstances.	• Results of file monitoring including suitability letters. • Mystery shopping/consumer research and feedback.	• High level of accuracy/appropriate advice provided to customers. • High proportion of customers giving feedback understand why the product sold to them was suitable for them. Customers understand their eligibility to claim on insurance products.
5. Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect.	• Consumer feedback questionnaires. • Complaints –Reasons & Outcomes. • PI Claims – Reasons & Outcomes. • Claims repudiations.	• High proportions of customers confirm that they had realistic expectations and that these were met. • No themed issues from root-cause analyses. Where themed issues are identified action taken is identified and reported.
6. Consumers do not face unreasonable post-sales barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.	• Complaints data. • Claims data for protection products.	• No themed issues from root-cause analyses. Where themed issues are identified action taken is identified and reported. • Claims are handled within agreed service standards. • No themed issues from root-cause analyses. Where themed issues are identified action taken is identified and reported.

Examples of good and poor practice in relationship-managed firms

Introduction

In assessing firms' MI we have considered if appropriate MI or measures are in place to test whether firms are delivering the fair outcomes. Our considerations have included:

- Senior management oversight and approach
- Appropriateness and quality of measures used and the analysis and decision making based on these measures

This Annex is structured as follows:

Section 1 – examples of good and poor practice we have seen relating to firms' overall approach to, and senior management oversight of, MI which are likely to help or hinder firms in demonstrating whether they are treating their customers fairly.

Section 2 – summary examples of good and poor practice measures received by senior management arranged here by TCF Outcome, which are likely to help or hinder firms in understanding the outcomes they are delivering for their customers and whether these are fair.

Section 3 - detailed examples of good practice MI again set out by TCF Outcome at senior management and working levels within a firm's business. Some examples include further information on the summary measures received by senior management.

Even though a minority of relationship-managed firms met the March deadline on time, the majority of examples included in this Annex are good practice because we want to focus on providing practical examples to help firms establish appropriate MI and measures to demonstrate the fair treatment of customers. But we have also included common examples of poor practice to help firms recognise areas in which they may be able to make improvements. We strongly encourage firms to consider the examples in the context of their own business model.

The examples of good practice in Annexes 2 and 3 are illustrative. They are not minimum standards nor do they amount to guidance under the Financial Services and Markets Act (FSMA).

Each individual measure is unlikely by itself to be sufficient in evidencing a whole outcome. Each measure may be relevant to more than one TCF Outcome.

Whilst the examples have been observed in particular firms, we consider that many are applicable across a range of sectors and business models. Many of the examples are relevant to product providers and distributors and some are relevant to service providers.

The examples do not seek to be comprehensive i.e. firms may well need other measures not detailed here to demonstrate an outcome or have other measures that are more appropriate to their specific business model or sector.

It is not necessarily the case that firms will need to use all of the measures we have provided in this publication, nor do we expect firms necessarily to highlight their mapping to the specific TCF Outcomes within their MI. But an FSA supervisor may ask a firm to explain how their MI – however they have chosen to organise it – maps to the TCF Outcomes, in order that the firm and supervisor can understand the coverage of the MI. These examples should not be construed as recommending use of a particular approach to MI.

TCF should not generally require the creation of substantial amounts of new information – the relevant information may already be available in the form of current MI the firm collects. In many cases, firms may analyse existing MI to demonstrate fair treatment by considering "what is the MI telling us about how fairly we treat our customers?"

Firms of all sizes will find examples which can be applied (with appropriate modification) to their business. Of course, MI or other measures should be proportionate to the size and complexity of the business and cost effective. For example, in a small firm with few lines of business where senior management are likely to be much closer to the day-to-day interactions with customers, the MI will be simpler than those in a much larger firm or a firm whose operations are more complex.

For MI to demonstrate fair treatment we would expect it to focus on how far a firm is delivering fair outcomes rather than measuring processes. Information on process can be helpful – and therefore we have included some examples here – but process measures are unlikely to be enough to demonstrate delivery of fair outcomes without other supporting evidence. We would encourage firms to consider carefully the extent to which their measures of process are measuring outcomes.

1. Oversight and Approach

The way in which firms oversee MI is an important factor in their ability to demonstrate that they are treating their customers fairly. This section sets out examples of good and poor practice we have seen relating to firms' overall approach to MI and senior management oversight.

Firms should be able to demonstrate that they use appropriate and comprehensive MI. It is also important for firms to demonstrate that they have sufficiently robust controls to ensure that MI is produced, analysed and reported in the right way and by the right people, including escalation to the relevant individuals. MI and measures should be reviewed over time to ensure that they are still appropriate and continue to effectively inform senior management.

The examples provided within this section reflect good practice in the general development and handling of any MI, not just MI used to measure fair treatment. But we also observed in our assessments that the common themes here were also those that distinguished firms that met the deadline from those that did not.

1.1. Good practice

- **Senior management oversight.** The quality of senior management oversight is key to ensure that TCF is being monitored effectively and actions are being taken as appropriate. Senior managers' oversight includes clear accountability for reviewing, challenging and acting on the MI to ensure that fair treatment is being achieved. For example:
  - The top-level MI pack seen by senior management was very clearly aligned to the packs regularly produced at working level.
  - For each business unit, the risks to the fair treatment of customers were reflected in the risk management framework. Appropriate senior management reviewed the risk report in conjunction with high level MI on a monthly basis.
  - Regular review of working-level MI packs by firm's appropriate level of senior management to challenge data integrity, validity of measures and appropriateness of escalation routes.
  - Middle managers were regularly challenged by senior management about aspects of their working MI. Comments from senior management were cascaded back to the working level.
- **Embedding TCF within the business.** Senior management decision making can be facilitated where TCF MI is embedded within the business. We have found that TCF and TCF MI are more easily embedded into a firm where the strategy and controls of the firm are consistent with fair treatment. For example:
  - The firm's strategy was consistent with fair treatment of customers and senior management included fairness measures in monitoring the delivery of the strategy.
  - Planned compliance audits from the annual compliance plan explicitly contained testing of TCF Outcomes, thus reinforcing the embedding of fairness into the firm's general oversight mechanisms.
  - Decision making took appropriate account of customer treatment throughout a firm from junior to senior management. This was supported

with high-level MI built up from individual teams or business units through to senior management level. A number of additional overarching measures provided aggregated MI across the firm.

- **Accountability.** Accountability for TCF must be clear and must be at an appropriate senior management level. For example:
  - Delivery of the firm's strategy including fair treatment was structured around high-level customer objectives and a senior manager was accountable for each of the objectives. This accountability was clearly set out and understood by individuals at all levels of the firm.
  - For every measure that failed to reach the required target, commentary was provided and actions were allocated to specific individuals.
- **Ongoing improvement.** Firms with strong oversight conducted a periodic review and challenge of their approach to MI to determine whether the measures used were appropriate to track delivery of the outcomes. For example:
  - Periodically assessing MI for its ability to measure relevant fair outcomes and identifying where measures were insufficient or missing for particular outcomes.
  - Consideration of a wider range of sources of evidence such as staff, controls and customers to provide a fuller picture of delivery of fair outcomes.
  - Rather than just challenging unsatisfactory performance, where the performance against a particular TCF measure was rated as satisfactory, the performance was challenged at senior management meetings on a regular basis, to determine whether it reflected the true status of the measure or whether the measure was sufficiently challenging. An audit trail was kept of measures and related performance that had been changed as a result of this challenge.
- **Ease of use.** Good examples of MI are presented clearly and can be easily understood. For example:
  - MI presented in such a way that the firm's view of its treatment of customers is absolutely clear and is not open to individual interpretation or misunderstanding. Measures are well defined and there is a clear standard and result with appropriate commentary.

1.2. Poor practice

- **Lack of appropriate MI.** Although reporting does not need to be presented by consumer outcome, measures should be checked so that they capture performance of the firm for relevant outcomes. Even where all TCF Outcomes are relevant to a firm, it is sometimes the case that firms fail to evidence their performance against all such outcomes. Further, firms are often not undertaking sufficient identification of the TCF risks within their business and how these relate to the outcomes, to ensure the risks are being managed through the MI. Many firms did not conduct sufficient testing of data to determine whether risks within the business would be captured by the collection, analysis and aggregation of the MI.

- **Lack of appropriate commentary and qualitative data.** Appropriate commentary and qualitative data can bring to the attention of senior managers specific TCF issues within a firm and allow greater challenge. However, senior management are often unclear on what particular measures might tell them about their TCF performance and which measures provide appropriate evidence of whether firms are treating their customers fairly. It is important that senior management understand the reasons for performance achieved. There is often a failure to analyse the TCF implications of issues that arise within the high-level MI. For example, firms might collect MI around the number of files that did not pass quality checks, but not analyse what the failures indicated about treatment of customers.

- **Insufficient detail in senior management MI.** We recognise that senior management need to receive summarised MI and other escalation or reporting mechanisms may exist. However, issues that are material to the firm's fair treatment of customers are often lost in summary reporting and therefore senior management are not being alerted through the MI. For example, we have seen firms where the higher level MI may show that the overall quality and suitability of the firm's advice is acceptable. However, on drilling down there are material issues with advice on certain products or within business areas that are not highlighted in the high level MI. Even where these issues are being addressed at the working level, senior management need to be aware of their existence.

- **Limited consideration of TCF Outcomes at the firm level.** Firms often struggle to collate evidence of results and actions at the working level within the business and escalate them to the appropriate level of senior management to enable them to make a judgement of the firm's overall treatment of customers. For example, firms typically collect MI around the results of individual product reviews. Collating the results of these reviews and presenting an aggregated set of results to senior management could provide evidence of product design fairness overall.

- **MI on processes rather than outcomes.** Firms often over-rely on MI gathered around completion of processes. Whilst this can be helpful, it may not provide insight into the outcomes or risks that the processes are trying to address. For example, using MI which simply records the number of financial promotions that are approved may not provide an insight into the consumer outcomes that are – or are not – being achieved by the financial promotions.

- **Lack of challenge to TCF MI.** Senior management often do not challenge measures which suggest a good performance. While we recognise that senior managers would wish to rectify poor performance as a priority, the challenging of measures which look acceptable will be key to ensuring the integrity of the firm's MI.

- **Lack of performance targets and trend analysis.** Firms are often unable to clearly articulate what acceptable TCF performance is or explain the reasoning behind their targeted levels of performance. We expect firms to set themselves stretching targets, to challenge themselves on their appropriateness and to understand and explain why particular targets have been set. We recognise that unfair outcomes will sometimes occur, even when TCF is fully embedded into the business, but firms must ensure that prompt action is taken to remedy these. We also noted a general lack of analysis of longer term trends and firm progress with regards to their performance against the TCF Outcomes.

- **Over-reliance on customer satisfaction.** Firms are frequently placing too much reliance on customer satisfaction and insufficient focus on the fair treatment of consumers. Whilst customer satisfaction can provide some useful insights it is not a measure of fair treatment. Firms also frequently place reliance on the customers' view of whether they have been treated fairly, which may not be a reliable measure of whether fair treatment is actually occurring.

- **Data presented by some firms has not been robust or accurate.** In some cases firms' MI has not actually been accurately measuring what it purports to measure.

2. Summarised examples of Senior Management MI

This section sets out examples of good and poor practice measures that we have seen used in senior management MI. The examples are arranged here by TCF Outcome.

Outcome 1: Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.

Good practice

- Senior manager interactions with customers (such as customer forums or call listening) with any insights considered and fed back to the business to make TCF improvements.

- Monitoring the involvement of senior management in promoting a TCF culture within the firm such as internal communications in the form of presentations or newsletters.

- Monitoring the proportion of sales staff bonuses withheld as a result of issues arising from quality checks. A low number of bonuses withheld could be indicative of a strong culture, but only if supported by robust controls which ensured that quality issues were fully taken into account when considering bonus allocation.

- Staff feedback from surveys or other sources which capture views, such as whether they thought the firm treats its customers fairly and whether they would recommend the firm to family and friends.

- Staff understanding and awareness of how to ensure fair treatment of customers is monitored by measuring the proportion of staff who had attended fairness training courses and passed a test at the end of the course.

Poor practice

- Whilst many firms have included qualitative measures within their remuneration structures, there was usually very little measurement or analysis of the actual to forecast payments of related bonuses.
- Reliance on measuring numbers of staff completing fairness training without some form of testing of staff knowledge and understanding, to provide evidence of TCF culture. This may not provide insight into how well the training helps staff to understand how to ensure fair treatment of customers in their day-to-day roles.
- Reliance on MI indicating low volumes of complaints as the only evidence of TCF culture. Whilst this could be a positive indicator, it is not sufficient on its own as it relies on consumers to judge fairness and bring issues to the firm's attention.

Outcome 2: Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

Good practice

- Reporting on the fairness implications of product reviews which analysed results of consumer research, customer analysis, retention, use of product features, product related complaints and product performance. Actions taken included design improvements and product withdrawal.
- MI around actual vs forecast sales of products and services to identify and investigate inappropriate targeting. Analysis was typically conducted against type of product or service, customer type, channel and distributor.
- Customer feedback, to determine if needs are being met and whether products and services were targeted appropriately. Feedback could include product and service related queries and complaints (with root cause analysis), comments from customer exit surveys or consumer research.
- Intermediary and distributor feedback on product or service design. Comments were reviewed by senior management and fed back into the design process.
- Customer analysis to assess if actual customer profiles were consistent with profiles of target groups.

Poor practice

- Firms often do not capture MI around the appropriateness of the design and targeting of existing products as well as they do for new products.
- Some firms rely upon MI stating the number of products that are approved where this approval is based on insufficient consideration of the fair treatment of customers.

- Some firms that offer services rather than products did not think this TCF Outcome was relevant to them and did not produce MI to measure if services meet needs or if they are targeted appropriately. Measures indicating that the firm is meeting consumer needs in a targeted way are still appropriate.

Outcome 3: Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale[7].

Good practice

- Measuring the clarity of information provided to customers through checking Key Facts Illustrations, call monitoring and suitability letters.
- Measuring activity against standards of completeness and timeliness of post-sale customer communications.
- Gaining views on the clarity of planned communications so that the firm can assess the likely messages that consumers will take from marketing or other contact activity.
- MI around complaints and queries relating to communications and analysis of root cause and trends.
- Post-sales welcome calls to measure at a high level whether customers understood the key risks and benefits of products they had bought.
- Measurement of number of intermediaries contacted who confirmed that they had received the appropriate product information.
- Results and analysis of the TCF implications of quality assurance checks on financial promotions. Tests include clarity of literature, explanation of risks and explanation of product features.
- Any feedback to providers from intermediaries on the quality, clarity and suitability of product and promotional information.

Poor practice

- Heavy reliance on post-sales information such as persistency, retention, complaints and claims success as evidence of clear communications. Whilst this can offer valuable insight, this is data collected after the point of sale and firms should consider what evidence they have that information provided to customers is clear before being issued.

7 It is important that consumers are able to take informed decisions based on the information and explanations they receive - this does not mean they need to understand the detailed workings of a particular product but they should know the main risks, benefits and costs involved and know what actions they need to take. Where firms provide information for consumers on products or services it is difficult to see how firms could evidence that they are treating their customers fairly, if that information is not capable of being understood by the consumers it is intended for or who are likely to receive it. This not the same as requiring evidence of a consumer's actual understanding.

- Lack of insight indicating that customers are being kept appropriately informed such as analysis of customer response to communications or records of key communications being provided (or exception reporting to highlight where this is not the case).
- Insufficient evidence of quality checking of communications after the point of sale.
- Insufficient focus on gathering and analysing MI around queries, such as requests for clarification, which might indicate that a particular communication was unclear.
- Over-reliance on measuring the number of financial promotions or customer communications reviewed for clarity. This in itself does not provide adequate evidence of the outcome as a whole. Analysis of the proportions judged to be unclear, the reasons for this and changes made, together with monitoring of consumer responses, would provide more robust evidence. Firms need to challenge themselves that the sign off process includes TCF considerations and that they have sufficiently robust MI to identify TCF issues in customer communications.
- Reliance on only measuring the volume of non-advised sales, and number of files checked, rather than also considering quality issues, such as identifying the proportion of files failing checks and the reasons for this.

Outcome 4: Where consumers receive advice, the advice is suitable and takes account of their circumstances.

Good practice

- Results and analysis of the TCF implications of independent quality checks, including file reviews, observation of sales and call monitoring, to determine whether the customers' circumstances were adequately taken into account before product recommendation.
- Results and analysis of the TCF implications of mystery shopping exercises. Tests included suitability of advice and whether the adviser had sufficiently taken the mystery shopper's circumstances into account.
- Where advice forms a part of the services offered, analysing complaints relating to advice by volume and/or as a proportion of total complaints. Root cause and trend analysis conducted against complaints allowed senior management to identify recurring issues.
- Analysis of sales patterns by product/service, whether advised/non-advised, product mix, individual adviser or team and the TCF implications of trends identified.
- Results and analysis of the TCF implications of cancellations, not taken up rates and persistency or retention, to identify any advice-related TCF issues.
- An activity report is run that analyses the number of trades within a portfolio in relation to the number of holdings and the size of the portfolio. Unusual patterns are investigated.

- Identification of potential commission bias through the measurement and analysis of sales volumes, product and/or provider mix and bonuses paid to individual advisers.

Poor Practice

- MI that measures quality of advice but where reasons for failure such as unsuitable advice or incomplete documentation are grouped together. Senior management are then unable to easily assess if the key risk of unsuitable advice is occurring.
- Insufficient analysis of why files have failed quality checks and lack of trend analysis which could help to identify recurring issues within teams, or amongst individual advisers.
- Lack of consideration of other measures that are available and might indicate advice issues such as product and/or provider mix or the proportion of non-advised sales.

Outcome 5: Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect.

Good practice

- Measurement of whether product performance is likely to have met with expectations which were communicated to the customer at the point of sale (i.e. 'it does what it says on the tin'). In practice, this might include measuring performance against the terms of the product and some firms compared performance to alternative products, benchmarks or competitors over an appropriate period of time. Senior management would then determine the appropriate actions to take, if any, given continued performance that was likely to be below expectations.
- Measurement of customers' experience of service levels, such as responsiveness to queries or acting on instructions.
- Claims analysis such as the number of actual claims compared to expected claims, or the number of rejected claims as a proportion of the total number of claims. Root cause and trend analysis of rejected claims.
- Root cause and trend analysis of complaints related to service received or product performance.
- Collation and analysis of retention rates and root cause analysis of lapses, cancellations and clients leaving. These measures can be used to evidence several outcomes, but are relevant to Outcome 5 when they are used to identify where there are issues with service or product performance.

Poor practice

- Too much reliance on complaints data alone and a lack of consideration by firms over the expectations that they have set with consumers and evidence of how they have met these expectations.
- Reliance on customer feedback from automated surveys where the member of staff could choose whether or not to put a customer through to the survey and hence bias the sample.
- Over-reliance on the results of customer surveys which were sent out at a specific point in time, rather than also gathering MI on other key aspects of the customer experience.
- Lack of insight from interactions with and information received from intermediaries and distributors.

Outcome 6: Consumers do not face unreasonable post-sales barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

Good practice

- Results and analysis of the TCF implications of surveys which asked successful and unsuccessful claimants and complainants how easy it had been to make a claim or complaint.
- Results and trend analysis against established post-sales service measures, including timeliness on processing claims, complaints or switching and transferring out, with a focus on the customers' interests being met.
- Measure of speed of payment in relation to product maturity or redemption.
- Number of complaints which passed quality checks as a proportion of the total number of complaints checked.
- Proportion of customers incurring early exit penalties, measured against the firm's expectations, and monitored together with customer feedback on this issue.

Poor practice

- Over-reliance on claims and complaints volumes and not enough analysis of barriers to claiming or complaining such as periodic internal checks. For example, assessing how easy it is for consumers to complain and making this easier may actually result in an increase in the number of complaints received.
- Over-reliance on volumes of product transfers and switching without evidence of how easy it was to switch or transfer. Very few transfers or switches may be indicative of fair treatment of customers or of major post-sale barriers. High levels might be indicative of churning, potentially resulting in poor customer outcomes.
- Over-reliance on listing the number of ways in which customers could contact the firm, rather than analysis of whether customers were able to engage with the firm and obtain a satisfactory and timely resolution to their post-sale requirements.

3. Detailed examples of good practice by TCF Outcome

This section gives detailed examples of good practice MI set out by TCF Outcome, at senior management and working levels within a firm's business. Some examples include further information on the summary measures received by senior management (as included in Annex 2B, Section 2). The examples were observed during assessments of relationship managed firms.

Outcome 1

Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.

Senior management involvement

- Senior managers attended customer panels organised by local branches. They used the feedback from customers to challenge colleagues on fair treatment of customers and to make improvements.
- Senior managers attended staff induction courses to deliver a presentation on the importance of fair customer treatment to the firm and on what it should mean for staff in their day-to-day roles. The proportion of courses attended by senior managers was measured. Their involvement in customer fairness activities along with the communication of key TCF messages in the staff newsletter were monitored.
- Senior managers spent one day a month undertaking call listening in the sales call centre, obtaining staff feedback and holding question and answer sessions with staff. They also facilitated customer and staff discussions on TCF issues. The findings from these monthly sessions were aggregated and reported across the whole business to raise awareness of any issues. They took action on the basis of the results.

Training and competence

- All sales staff were required to complete periodic knowledge health checks in the form of 30 minute interviews to check they understood and applied fair treatment principles correctly. A report was produced for senior and middle management that summarised the interviews and suggested corrective action where weaknesses had been identified.
- A record was kept within the business of the number of staff who completed training in how to deliver fair treatment to customers and the score they achieved in exercises designed to test their understanding. Those who failed to achieve the required score were provided with extra support and required to re-take the test until they passed.
- MI was collected around the number of outsourced call centre staff who had passed induction training tests on the fair treatment of customers. The tests were of the same standard as those completed by in-house staff. The MI was used to ensure that those who failed the training retook the test.
- MI was analysed which demonstrated how staff's knowledge and awareness of TCF had moved over time, to evidence continuous improvement and identify any specific areas requiring further attention.
- At a team level, workshops were conducted to increase awareness amongst staff of what was expected of them in relation to TCF. The output from each workshop was captured in a team TCF charter. Each team produced its top ten TCF commitments, along with an action plan which was reviewed at each team meeting. The firm measured the number of teams who had completed the action plan.

- Measures were maintained of the proportion of staff whose performance objectives contained fairness goals and progress against these goals was monitored. The measure was contained in the high level MI.
- A fairness cultural assessment was conducted of all Appointed Representatives by asking questions to assess their engagement with the TCF initiative. At working level, the results led to each representative being given a risk ranking. Those assessed as higher risk were accompanied more frequently on visits until their risk rating was reduced.

Staff feedback

- Staff were encouraged to give feedback to senior management on fairness issues. This could range from concerns that TCF Outcomes were not being met, to recording examples of good TCF practice. The information was collated into regular reports, which were analysed and actioned by management.
- A regular staff survey included specific fairness questions, including whether staff:
  - felt the customer experience was improving;
  - felt the firm's appraisal system encouraged them to treat customers fairly; and
  - would recommend the firm to their family and friends.

The scores for each fairness question were aggregated and given a rating. The results were included in the high-level MI and year-on-year trend analysis was conducted.

Reward

- Inclusion of qualitative factors into remuneration schemes for advisers and sales staff. These included:
  - quality of advice;
  - not taken up rates;
  - persistency or retention/cancellations;
  - whether all relevant information was provided to the customer, assessed through call listening and file checks;
  - complaints;
  - product mix; and
  - feedback from customer surveys.

The high-level MI included a metric for the number and percentage of staff whose bonus had been affected in full or in part by the quality measure and the reasons why. This was broken down by different type and level of employee.

Outcome 2

Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

Products designed to meet customer needs

- A local change committee was used to sign off changes to products. It used specific customer-focused insights, such as customer analysis or consumer forums, to indicate if the changes were fair to customers. A target was set for the proportion of product changes made as a result and the number was monitored.
- Scenario testing was carried out to assess the risks of products for different client groups. The results were collated, fed back into the product design process and used to inform the drafting of promotional material.
- Feedback was gathered from forums at which specialist practitioners and product designers from providers met with intermediaries to discuss the segments of the market being targeted, the risks and benefits associated with products, the risk profiles and needs of customers and the quality, clarity and suitability of product and promotional information. Forums along these lines have directly influenced product design and the marketing strategies of both producers and distributors.
- The fairness of all products was assessed through an annual review which included:
  - usage of product features;
  - attrition rates;
  - persistency;
  - complaint trends;
  - cancellations;
  - competitor comparisons; and
  - consumer research.

Issues were reported to senior management. If a product was deemed unsuitable, or unfair, after analysis, suggestions were recommended for improvement, or the product was withdrawn. The firm could demonstrate that one product had been replaced pending a fuller review of its fairness.

Product targeting

- Measures of target compared with actual sales and persistency were used. Root cause analysis was conducted of early and mid-term cancellations to determine whether products had been cancelled because they were inappropriately targeted. The results were fed into the product design process. This information was analysed by product, customer type and distribution channel in order to identify specific product targeting issues. There was evidence that products had been withdrawn or changed as a result of this analysis
- Customer profiles for new business sold were measured against the target profile to ensure they matched, using demographic data and attitude to risk.
- A risk ranking was conducted of all existing products, taking into account issues such as product performance and market conditions. This information was mapped to clients' stated risk appetite to ensure that products were appropriately targeted. Changes in the ranking were reported quarterly to the management in marketing and business development.
- Reasons for the rejection of claims were monitored. If it was established that claims had been rejected because the wrong product had been bought, either the cost of the product was refunded to the customer, or the claim was paid, whichever was the higher amount.
- An online assessment automatically rejected applicants who could not demonstrate that they had sufficient market knowledge to use an execution-only stockbroking service. MI on the number of applications rejected and the reasons why was produced for every stage of the application process.

Outcome 3

Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.

Financial promotions

- Quality assurance was conducted against all financial promotions, assessing factors such as clarity, whether key features were adequately explained, and whether risks were clearly articulated in the document. The number of promotions which failed to meet the expected standard was measured, along with the reasons for failure and any changes made as a result. This information was included in the high-level MI and trends were monitored on a monthly basis.

Quality of communications

- The following measures were used to demonstrate that their communications were clear during the sales process:
  - number of Initial Disclosure Documents (IDDs) issued that adequately reflected the proposed service;
  - number of Key Facts Illustrations (KFIs) judged to be clear and appropriate;
  - number of clients issued with a compliant menu; and
  - proportion of suitability letters verified as clear.

The measures were collated onto the firm's high-level MI, which was seen by senior management. Where scores fell below set targets, management reviewed the issues and took action.

- Consumer research was conducted on communications before they were issued, to test their clarity and comprehensiveness. Consumers were shown the material, asked for their first impressions, asked what they believed the key messages were, and then tested whether they had understood the material.
- Information was collected about complaints and queries relating to communications and root cause analysis carried out.
- Quality listening was conducted on a proportion of sales calls. Calls could be failed for a number of reasons, including failure to adhere to the script, lack of clarity when explaining products or providing advice on non-advised calls. Call centres collated MI around the number of calls that failed and why. Action was taken to retrain staff who failed to meet the required standard. Line managers might contact the customer, to ensure that any error or omission was corrected, and where necessary to arrange a refund of any premium taken.

Communication with intermediaries

- The sales teams routinely contacted intermediaries to ascertain whether they had been provided with the appropriate product information. MI collected around this was fed back to communication teams at working level.
- Monthly forums were held where product information and related marketing material were explained to intermediaries, ensuring that they understood the range of products, their risk profiles, etc. A record of attendance at meetings was used to monitor that intermediaries had been presented with the information.

Post-sales information

- Detailed research was conducted on a wide range of UK Collective Investment Scheme products. All funds were given a risk grade, which was published online, so that customers were able to form a rational view about performance expectations and risks. Particularly poor performing funds were monitored through regular reviews. If a customer decided to invest in one of the poorly performing funds, the head of investment advisers would be alerted and the customer sent an email to inform them of the firm's view of the fund.

Post sales checks

- A sample of customers was contacted post-sale to assess their understanding of communications and the product they had bought, and their experience of the sales process. For example, the proportion of customers who had not understood the Initial Disclosure Document was measured. This information was included in the high level MI and was used to clarify product documentation.
- The number of mortgage redemptions was monitored and customers were contacted, to ascertain whether they were leaving because of poor communications after the point of sale. Root cause analysis of reasons for redemption was conducted and recurring issues highlighted to senior management.
- Measurements were maintained of the number and results of quality checking of post-sales communications (such as notification of changes to products and upcoming insurance policy renewals) which were designed to ensure they were clear and timely.

Complaints

- Root cause analysis of complaints was conducted to identify instances where communications had not been clear. In most cases, the analysis had led to specific action being taken within the business, including letter writing courses, or further staff training. The complaints data was included in the high level MI.

Outcome 4

Where consumers receive advice, the advice is suitable and takes account of their circumstances.

Quality of advice

- The outcomes of file quality or sales call checks were measured on the basis of a stated proportion of sales. Criteria included whether:
  - customer needs were appropriately assessed;
  - product risks were clearly explained;
  - reasons for the advice were clearly explained;
  - the customer's circumstances were taken into account; and
  - all required documents were appropriately completed and included in the file.

Analysis was included in the senior management MI pack, and was broken down by product. A rating was given for each measure and trends were analysed on a monthly basis. At a lower management level, the quality measures were broken down by individual advisor. Where issues occurred, line management arranged additional training or remedial action to improve the performance of the adviser.

- The quality of sales calls was assessed by peers as well as managers. The peers listened to a number of calls live. Immediate feedback was given to the sales person, giving actions for improvement. MI was collected around the number of calls which had given rise to an issue. Where a specific issue was raised more than once, action was taken at team level.
- The following indicators were captured to measure quality of advice:
  - not taken up rates;
  - cancellations during the cooling-off period;
  - persistency by product; and
  - complaints relating to advice. For example, where advice forms a part of the services offered, analysing complaints relating to advice by volume and/or as a proportion of total complaints. Root cause and trend analysis conducted against complaints allowed senior management to identify recurring issues.

These measures were typically included in the high-level MI reviewed monthly by senior management. Measures were analysed and rated and trends were analysed monthly. TCF issues emerging from the measures were actioned.

- Sales flows and volumes were collated and matched against expectations and targets, especially relating to product mix and provider mix. Where advised sales were higher than expected in particular areas, management investigated to ensure that the performance was not the result of commission bias, inappropriate bonuses paid to advisers or mis-selling.
- A monthly programme of mystery shopping was established to test the suitability and quality of advice given by sales staff. The shoppers tested a range of issues, including

the quality of the needs assessment, clarity of information relating to the products on offer and whether or not the risks were explained adequately. Results were broken down by type of product and region and collated into a 'headline' document, which identified trends and suggested areas for improvements. The document was seen and analysed by senior management and actions were taken on the results.

- The same controls were applied to outsourced telesales staff as to in-house teams. The performance of outsourced staff was closely monitored through call and file quality checking by management, and the outsourcer submitted the results to the contract manager. The results of both the in-house and outsourced measures were captured in the high-level MI, which was reviewed monthly by senior management. Changes were made to scripts and training programmes used by the outsourcer as a result of the issues identified. The evidence demonstrated that the number of complaints had declined.
- The portfolios of clients receiving investment advice were reviewed and the results scored against a number of factors, including suitability of advice and clarity of communication. Trends were analysed and where the quality of advice was found to be substandard for particular portfolios, action was taken.
- All advised trades on investment management accounts were reviewed to identify potentially unsuitable activity, such as the purchase of shares that were not on recommended lists or not in line with clients' risk appetites; or different clients buying and selling the same stock. Unsuitable trades were reported to management for action.
- An activity report analysed the number of trades within portfolios over time in relation to the number of holdings and the sizes of the portfolios. It investigated both unusually high and unusually low levels – the former as a potential indicator of overtrading or a high risk investment strategy, the latter as a potential indicator that the portfolio was not receiving sufficient attention.

Customer circumstances

- Before any advice was given, the computer system prompted the adviser to update the customer's details and obtain up to date information on the customer's circumstances. Compliance checked that this was being done and compared the details against the advice given and customers' holdings. The results were provided to senior management.

Quality and experience of advisers

- Scoring systems allowed senior management to identify where the levels of experience in teams might not be sufficient. A score was allocated to each staff member, according to their level of experience. At a working level, sales managers saw MI relating to each team and were able to re-allocate staff when the score indicated that the team mix might be inadequate to ensure that suitable advice was being given.
- Basic performance records were kept for each adviser where a number of elements (suitability of advice, file quality, complaints, advice mix, product mix and knowledge tests) were scored and recorded. Typically, these records would also contain line manager comments and an action plan if issues of concern had been noted. These records were fed into the high-level MI, enabling senior management to identify recurring trends and issues, including commission bias, or mis-selling.

Outcome 5

Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect.

Ongoing monitoring of performance

- Measurements were made of the proportion of claims declined and the proportion where the claim was met in full. The proportion of complaints relating to shortfalls in claims payments was also measured and analysed by product line. The measures were collated and included in the high-level MI. Root cause analysis was carried out, trends were analysed monthly, and action taken on issues of concern.
- TCF-related measures relating to product performance were collated and analysed, including:
  - industry comparisons;
  - product performance testing in a variety of market scenarios;
  - actual performance against expected performance;
  - investment performance to monitor the risks of continued underperformance;
  - retention;
  - queries and complaints; and
  - intermediary feedback.

Each product was given a TCF risk rating, which was reviewed at the appropriate senior management level.

- The numbers of ex-gratia payments made on rejected insurance claims were monitored to track potential issues with product performance, and root cause analysis carried out to investigate the reasons for making the payments. The results were fed into the high-level MI.
- Samples of claims, surrenders and maturities were reviewed to assess whether the payouts were consistent with fair treatment.
- The trading frequency within clients' accounts was monitored, both by value and by volume. These were measured against thresholds and both overly low and overly high activity was investigated.
- The relative performance of managed portfolios was measured and analysed, and the reasons behind those that were significantly ahead or behind the rest were investigated.
- All investment portfolios managed were reviewed to check whether they were in line with predetermined asset allocation limits and the results compared against a qualitative review of the actual holdings by other fund managers within the allocations.

Service Standards

- Analyses were conducted of the results of feedback from customers on their experience of service levels, such as responsiveness to queries or acting on instructions.
- The reasons why customers transferred their products to other providers were compiled on a monthly basis. The commentary and qualitative analysis were reviewed by appropriate senior management.
- All rejected claims were referred to higher management for approval, to ensure that they had not been unfairly rejected. The number of and reasons for rejected claims was recorded in the firm's high-level MI and trends analysed on a monthly basis.
- Root cause analysis of complaints, claims, lapses, and cancellations was used to draw out issues relating to product performance or service received and refer them to the appropriate area of the business for action.
- The trading patterns of non-advised clients of stockbrokers were monitored to pick up any trends which might indicate any customers who did not fully understand market risks. They were then contacted to discuss their suitability to continue as clients.

OUTCOME 6

Consumers do not face unreasonable post-sales barriers imposed by firms to change product, switch provider, submit a claim or make a complaint.

Barriers analysis

- Analysis was conducted on a periodic basis to assess potential barriers affecting customers' ability to make claims and complaints or to transfer to other providers.
- Complaints from customers closing and switching accounts were analysed to determine whether there were any unreasonable barriers and the results included in the high-level MI with commentary around trends.
- Records were maintained of the number of times customers had to call to obtain a satisfactory resolution to their claims (average number of calls per customer per month). At working level, managers could drill down to establish whether issues had arisen with a particular team or adviser. The information was used to reduce barriers to claiming and was also provided to appropriate senior management as part of the high-level MI.
- Service standards were set for customer contact teams and their performance monitored to review how easy it was to make complaints or claims and the time taken to process them.

- The number of customers who began the claims process but did not pursue it was monitored and a survey conducted to understand why they were not claiming. On the basis of the survey results, action was taken to encourage customers to complete their claims, including sending reminder letters to those who had begun the process. Trend analysis also identified potential barriers to claiming.
- The speed of processing maturity payments was measured, to indicate the existence of potential barriers.
- The proportion of customers incurring early exit penalties was monitored against the firm's expectations and related customer feedback was analysed.
- Complaints were tracked and root cause analysis carried out. In particular Financial Ombudsman Service referrals were monitored and the number of referrals upheld tracked as a potential indicator of problems in complaint handling.
- Root cause analysis of complaints was used to identify instances of unfair contract terms which could constitute post-sales barriers.
- Results and trend analysis against established post-sales service measures, including timeliness on processing claims, complaints or switching and transferring out, with a focus on the customers' interests being met. Performance was then analysed to determine if barriers to activities were reasonable.

Customer experience feedback

- Regular customer complaints forums attended by senior management provided opportunities for customers to provide feedback on their experience of the complaints system.
- A record was maintained of the proportion of complaints dealt with that passed quality checks and the number which required re-working on a monthly basis. Bonuses for relevant staff took account of the number of complaints which had been well handled.
- Surveys were conducted to assess customers' experience of the complaints and claims processes, including processing times. Data were also collected on the percentage of claims settled within the service level and the number rejected, and analysed in the high-level MI.

Annex 3

Specific regulatory issues

Introduction

TCF underpins the FSA's work on consumer protection including much of our thematic work. In this section we have again looked at provider/distributor responsibilities and also at some of the issues in our Major Thematic Work Plan for 2008/09 where firms may benefit from sharing relevant MI measures.

The good practice measures in this Annex are examples we have seen firms use either in our March assessments or our thematic work. If appropriately targeted on the specific issues, we believe these examples can provide evidence on whether the issues are being managed effectively and hence whether fair consumer outcomes are being achieved. We strongly encourage firms to consider the findings of our thematic work and the issues and example measures included here. Included here are example measures from:

- provider/distributor responsibilities;
- fairness in consumer contracts;
- with-profits;
- mortgages;
- Payment Protection Insurance (PPI); and
- pension annuities: open market options.

Provider/distributor responsibilities

We have published a Regulatory Guide which sets out our view of the respective responsibilities of providers and distributors[8]. In this, we explained that providers and distributors should consider the impact of their conduct on the customer in the various stages of a product's life-cycle, or the various stages of provision of a service, where this extends across more than one legal entity. Depending on the precise nature of a firm's business, this could mean addressing the fair treatment of customers in the following stages: design and governance; identifying target markets; marketing and promotion; sales and advice processes; after-sales information and service; and complaints handling.

8 PS07/11: *Responsibilities of providers and distributors for the fair treatment of customers*, July 2007.

We have seen some good approaches from firms which recognise the responsibilities of providers and distributors in delivering fair outcomes to consumers and appreciate the importance of communication in achieving this.

However, a number of firms have found it challenging to collect MI to evidence that they are meeting all of their responsibilities under the Guide. In particular, several providers, from several sectors, have found it challenging to demonstrate how they are meeting the responsibilities that relate to the provision of information to distributors. They tend to have more measures in place to evidence that they are giving clear, fair and not misleading information to customers than they do for information provided to distributors. We would remind firms of their obligation under Principle 7 of our Principles for Businesses that 'a firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading'. We would caution all firms that provide information to distributors to think carefully about what they should do to ensure the information is sufficient, appropriate and comprehensible.

The following are examples of good practice measures for providers relating to provision of information to distributors:

- Testing the effectiveness of communications with intermediaries, through feedback, and drawing out any fairness issues.
- Providers' measures for the quality of their sales force who deal with distributors, such as the frequency of errors made in characterising the product.
- The results of discussions at intermediary focus groups designed to test product understanding.
- Capturing feedback from distributors from other sources – for example from conferences, seminars and forums.

The Guide also states that when monitoring distribution channels, a firm should review how actual distribution of products or services corresponds to (or deviates from) what was originally planned or envisaged. This may involve collecting and analysing appropriate management information so that the firm can detect patterns in distribution and assess the performance of distribution channels. A number of firms are taking insufficient action to meet this responsibility – too often they take the view that the existence of a distributor relieves them of any responsibility to the customer.

The following are examples of good practice measures providers have taken regarding this responsibility:

- analysing actual vs forecast volumes of sales by product, target group and distributor to identify unusual spikes and, where such spikes are found, investigating them; and
- monitoring key performance measures such as complaints, not taken up cases or persistency to detect any potential issues.

We have also previously published good practice illustrations for managers of UK authorised collective investment schemes relating to certain provider responsibilities[9].

Fairness of terms in consumer contracts

We expect firms to have fair terms in their standard[10] contracts with consumers. To do this, they need to comply with the requirements of the Unfair Terms in Consumer Contracts Regulations 1999 (the Regulations) and the principle of Treating Customers Fairly.

We recently reported that many of the firms whose contracts we reviewed still had unfair terms in their contracts[11]. This suggests that firms need to do more to ensure their contract terms are fairly drafted.

Examples of good practice we have observed include:

- regularly reviewing standard form consumer contracts for fairness to ensure they comply with the Regulations;
- reviewing contracts when complaints and cancellations are made or where there is evidence that terms may be unfair;
- reviewing all appropriate undertakings obtained by the FSA and the Office of Fair Trading (OFT) (as shown on their websites);
- reviewing other FSA information on unfair terms, eg thematic work, speeches and updates;
- monitoring alerts and industry guidance from trade bodies; and
- improving staff training to ensure staff meet the standards set out in product literature, including contracts.

With-profits

Our ongoing thematic and supervisory work has identified a number of issues around with-profits funds, and in particular closed funds, which we have previously highlighted in our publications and letter to CEOs[12]. A number of these issues have particular relevance to TCF both at the higher level, in relation to the governance arrangements of the funds, as well as issues such as clear policy holder communications. Some of the key TCF issues and risks that we have identified and which firms should monitor using appropriate MI include:

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9 'Treating Customers Fairly and UK Authorised Collective Investment Scheme Managers', January 2008

10 By 'standard', we mean all contracts that are not individually negotiated between a firm and consumers

11 'Fairness of terms in consumer contracts: a visible factor in firms treating their customers fairly', June 2008

12 Insurance Sector Briefing from November 2005 (Update on Closed With-profits Funds), September 2007, Dear CEO letter, Insurance Sector Briefing from May 2007 (quality of post-sales communications in the life sector and availability of ongoing advice to with-profits policyholders), Dear CEO Letter, www.fsa.gov.uk/pubs/ceo/ceo_letter_24aug04.pdf). Results of our review of processes, systems and controls for with-profits insurance contracts.

- That with-profits funds will be run without due independent challenge, leading to an inadequate degree of protection for their policyholders, and/or a failure to promote confidence among such policyholders.

- Policyholders will not benefit from the surpluses that should be distributed to them. Our rules require firms to distribute (or reattribute) any excess surplus, regardless of whether the fund is open or closed. We recognise that where a fund has closed to new business, fair distribution of any inherited estate becomes an issue. Particular challenges relate to how to distribute between different generations of policyholders to ensure a solvent run-off is maintained without unduly disadvantaging (or advantaging) policyholders whose policies mature in the shorter term.

- Firms may not provide policyholders with appropriate information to make informed decisions about their policy; this includes ensuring that all post-sales documents are clearly written, easy to understand and appropriately reflect issues of relevance to policyholders.

- Firms may apply inappropriate charges to customers.

- A particular challenge for closed funds is to have an investment strategy that meets both the expectations of different groups of policy holders and sufficiently safeguards the solvency of the funds.

The following are examples of good practice measures:

- MI demonstrating that the governance structures around with-profits funds are appropriate[13]; this might include the results of internal reviews of the governance arrangements.

- Number and type of queries on communications. Particularly relevant to with-profits would be the provision of further information when requested.

- Results of testing of consumer understanding of policy related communications.

- Results of checks on the quality and timeliness of communications on key product features.

- Actual asset mix of fund against agreed asset mix.

- Feedback from exiting customers.

- Monitoring of fund performance against expectation.

- The actual timeliness of payment of surrenders compared to service standards.

13 We published the results of a thematic review into the governance of with-profits funds in a Dear CEO letter 19 September 2007 http://www.fsa.gov.uk/pubs/ceo/with_profits.pdf

Mortgages

As we explained in the Financial Risk Outlook[14], we have several concerns with the fair treatment of customers in the mortgage market, although we appreciate that current market conditions are having an impact on the volume of business being written. We are currently undertaking thematic reviews in relation to responsible lending, arrears handling and repossessions and quality of advice processes on mortgages. We plan to report on these thematic reviews in a specific publication on mortgages in July 2008.

The following are examples of good practice measures:

- Results of quality of advice checking and root cause analysis of failure, including file checking, call monitoring and observation of sales.
- Actual vs forecast volumes of different types of mortgages sold to identify unusual sales patterns. For example advised vs non-advised, repayment vs interest only, high loan-to-value % and term into retirement.
- MI on the level of commission paid on advised sales to identify potential commission bias.
- MI on the reasons for mortgage default, analysed according to age profile or income verified vs income non-verified (including declared income or declared employment). The results of this analysis were used to test the appropriateness of a lender's affordability model.
- MI on persistency rates, analysed by advised and non-advised sales; this might uncover problems with the quality of advice.
- MI on the number of cases that are refinanced during the early repayment period and the charges incurred. Root cause analysis on the reasons for refinancing.
- MI on arrears and possession cases to inform changes to mortgage underwriting policies.
- MI to inform lenders' arrears handling policies and practices. This may include information on the success of 'arrangements to pay' and the outcome of court possession actions (e.g. if the courts are turning down a lot of applications for possession orders, the lender should ask itself whether its policy is leading it to take court action before other avenues have been adequately explored).

Payment Protection Insurance (PPI)

Our ongoing thematic work has shown a number of TCF issues across the industry, in particular in relation to the selling of PPI. Whilst there have been some improvements, in some areas, we have significant concerns that many firms may not be treating their customers fairly. Our September 2007 Thematic Update on The Sale of Payment Protection Insurance and our ongoing work has highlighted the following TCF related issues:

14 Financial Risk Outlook 2008, January 2008.

- Many firms are not making clear to the customer the price of the policy; for single premium policies, some firms are not clearly explaining that the cost of the policy will be added to the loan and interest paid on that amount.
- Firms do not give customers the basic information necessary to make an informed decision about the product.
- Firms need to give due consideration to suitability and establish whether customers are eligible to claim under different elements of the policy.
- Many PPI products do not appear to be well matched to meet the needs of the customers to whom they are sold. For example, where customers may not be eligible to claim under many sections of a policy which they have paid for. We believe that customers would generally benefit from a more flexible product that can be, and is, tailored to meet their needs and is targeted accordingly.

The following are examples of good practice measures:

- Carrying out root cause and trend analysis of complaints and monitoring proportions upheld and rejected, time taken to resolve complaints and the quality of complaint handling to assess if fair treatment is being delivered.
- From call monitoring and branch advice monitoring, number of key and non-key breaches in the sales process.
- Cancellations data distinguishing between those cancelling within the 30 day cooling-off period or outside the 30-day cooling-off period, cancellations of PPI when the loan is retained, reasons for cancellations.
- Number of claims and proportion rejected. Analysis of the reasons for rejection.
- Measures that answer whether types of PPI sold match the needs of consumers.
- Number of bonuses withheld as a result of issues arising from quality checks.

Pension annuities: open market options

Previously published material[15] has highlighted our concerns around the fair treatment of customers who are purchasing lifetime annuities using their pension fund. When buying a lifetime annuity, consumers should shop around to make sure they get the best deal. Our concern is that poor clarity of information provided for the open market option may discourage some who should from shopping around. We also have concerns that firms may not be highlighting important features such as guaranteed annuity rates.

15 Insurance Sector Briefing: Quality of Post-Sale Communications in the life sector and availability of ongoing advice to with-profits policyholders, May 2007 www.fsa.gov.uk/pubs/other/isb_quality.pdf

‘Future of life assurance: managing risks’, speech by Sarah Wilson, Director and Insurance Sector Leader, FSA, at the Institute of Economic Affairs, 15 May 2008, www.fsa.gov.uk/pages/library/communication/speeches/2008/0515_sw.shtml

We are also investigating claims that those policyholders who do switch providers by taking the open market option can face problems with the administration of this move, with sometimes significant delays around releasing funds. We will publish the findings of our review of whether firms are inappropriately delaying customers who wish to exercise their open market option and the quality of the MI collected around this issue in July 2008.

The following are examples of good practice measures:

- Data on the customers and the proportion of customers who have exercised their open market option. Firms should consider their place in the market and any penalties they impose or guaranteed annuity rates they may offer when considering what is a reasonable rate of switching.
- The results of firms' own reviews and testing of their consumer literature, including whether key messages have appropriate prominence and whether communications are clear and easy to understand.
- Measures of timeliness to pay open market option funds. Firms should be able to identify how long it takes them to pay funds of those who have exercised their open market option.

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