Financial Services Authority

Treating customers fairly – culture

July 2007

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Annex I: Culture framework (relationship managed)

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1 Key messages

- Treating customers fairly (TCF) is a cultural issue. It is only through establishing the right culture that senior management can convert their good intentions into actual fair outcomes for consumers. In our July 2006 publication[1] we included an outcome on culture which states that '*Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture*'.
- As firms will be aware, TCF is one of our priorities and, to be effective, they should be making it an integral part of their business culture. While we identified in our May 2007 publication[2] that an encouraging number of firms were at the 'implementing' stage of their TCF strategy, further progress is needed to reach the embedding phase. We now expect to see firms taking action to ensure a consistent delivery of fair consumer outcomes – to do this, firms need to consider their culture. The culture of an organisation drives the behaviours of its management and staff and their actions, which in turn will determine the outcomes for consumers.
- This publication sets out the culture framework (see Annex I) we have developed for supervisors to use when assessing the risk a firm's culture presents to treating its customers fairly. We have also developed a management behaviours framework (see Annex II) for smaller firms. The frameworks are based on factors or 'drivers' which we believe have a significant influence on behaviours in firms. The drivers we have identified will help firms to make the appropriate cultural changes to ensure the consistent delivery of fair consumer outcomes.
- Leadership at all levels sets the tone of an organisation, driving the behaviour of staff and the quality of decisions. Strategy sets the direction and priorities of the business and the focus for management. Controls, including management information (MI), are essential to satisfy managers (including senior managers) that the firm is delivering fair outcomes for consumers. An organisation's approach to performance management and reward drives the behaviour of staff and enables management to assess the quality of the performance of an individual.

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1 Treating customers fairly – towards fair outcomes for consumers, July 2006.

2 Treating customers fairly initiative: progress report, May 2007.

- We have also included examples of good[3] and poor practice from our visits to verify the frameworks and our TCF experiences. In the course of our work we have seen more examples of poor practice than of good. Many of the issues identified are straightforward, and we have raised some in previous TCF publications. We will consider how best to keep these examples updated so that they reflect current practice.

- We strongly encourage firms to consider the issues we have identified in this publication and think about how to use the frameworks to review their culture regarding treating customers fairly. While we have given specific examples of good and poor practice based on behaviours we have seen in particular firms, we think they are relevant to all types of business.

- To enable firms to take action and make the necessary changes, they will need MI to identify where they are failing to deliver fair consumer outcomes. We recognise that many firms have found identifying, collecting, and using MI for TCF challenging. We have included some examples of good and poor practice brings together on MI in this publication and to support firms in meeting the March 2008 deadline[4] we have also issued a separate publication on MI today[5]. This summarises relevant messages from other FSA publications with some new examples. We will continue to work on this difficult area as firms develop their own systems, including reviewing and challenging what firms measure and how they make use of MI. We will issue further examples in October.

- If we are satisfied that a firm has robust systems and controls and the senior management are reviewing and using reliable MI which demonstrates that they are treating their customers fairly, we will significantly reduce the level of testing we carry out on the firm's culture regarding treating customers fairly.

3 While we have given examples of 'good practice', these are not minimum standards and do not comprise formal guidance on the TCF Principle. In addition, some of the good or poor practice concerns compliance with, or breaches of detailed rules which we think have a significant impact on fair outcomes for consumers. Where this is so, firms must of course comply with those detailed rules.

4 In 'Treating customers fairly initiative: progress report', May 2007, we set a deadline for all firms to have appropriate management information or measures in place to test whether they are treating their customers fairly by the end of March 2008. By the end of December 2008 all firms are expected to be able to demonstrate to themselves and to us that they are consistently treating their customers fairly.

5 Treating customers fairly – guide to management information, July 2007.

2 Findings

- **Leadership** – While most senior management in firms can explain what treating customers fairly means to them and how this is reflected within the firm's strategy, middle management are often failing to deliver fair consumer outcomes within their business areas. We believe this is often due to senior management not giving middle management enough direction, and also failing to monitor them. Many of the examples of poor practice we have seen relate to an unreasonable expectation by senior management of middle management's ability to deliver fair consumer outcomes given the structure, pressures and incentives that they face. They also reflect failure by senior management and middle management to adequately monitor the delivery of good TCF behaviour and fair consumer outcomes. Where middle management feel empowered by senior management, both within their role and in their ability to challenge policies and procedures, there is less risk of unfair consumer outcomes.
- **Strategy** – Senior management frequently fail to allocate enough time and resources to deliver TCF when they are focused on other business priorities. We have identified situations where delivering fair consumer outcomes has been compromised because senior management oversight has become ineffective due to their involvement in the delivery of a new business initiative. In fact, consideration of TCF should be built into delivery of changes to the business.
- **Decision making and challenge** – Strategies, policies or procedures that deliver unfair consumer outcomes are not always challenged. We have identified firms where the senior management of a business unit or firm have not challenged a strategy that conflicts with TCF, for instance where it has been set by a parent company. This is often because of a fear that speaking up against an inappropriate strategy could have implications for the individual's remuneration or employment. In other situations, policies or procedures have not received enough challenge, as there was either not a formal process in place or the environment was not conducive to challenge by staff or customers.

- **Controls** – In general, firms are finding it hard to identify, collect, interpret and use relevant MI to monitor TCF effectively and to demonstrate they are treating their customers fairly. Even when appropriate MI is collected, many firms do not undertake qualitative analysis or provide effective commentary for those within the firm that receive the information.
- **Performance Management** – Performance management plans often do not include TCF-related objectives. Where we have seen TCF-related objectives, they often fail to explain clearly what TCF means for the individual's role or the behaviours and actions expected, and do not reflect the TCF strategy of the firm. Firms can fail to take appropriate action against individuals whose action (or inaction) has led to unfair consumer outcomes. We have seen several instances, in some cases at a senior level within the firm, where no action has been taken when poor TCF behaviours have been identified.
- **Reward** – Incentive schemes for senior managers often fail fully to recognise the influence senior managers have on the fair treatment of customers. Senior management incentive schemes often place heavy emphasis on targets associated with driving profit, increasing income, cutting costs or growing the business. There is often little consideration of how this can be achieved while still delivering fair consumer outcomes. We have seen situations where the fair treatment of customers has been included in individual objectives but the effectiveness of this target is questionable because it appears to be given insignificant weight compared to other targets.

3 Approach to our work

Background

In July 2006, we published a paper, 'Treating customers fairly – towards fair outcomes for consumers', which outlined the six outcomes we were looking to achieve. The first outcome states 'Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture'. In relation to this outcome, we stated that we intended to look at some of the organisational and management arrangements that may encourage or inhibit the move from senior management commitment to the consistent delivery of fair treatment of customers in all parts of a firm's business.

In our May 2007 publication on the progress of firms, we published the key cultural drivers we had identified at that stage. And we said we would give more details on the framework in July 2007, including examples of good and poor practice.

Developing the culture framework

The framework has been developed not only from our experiences in TCF, but also from our other work on specific themes, which give powerful information on the factors, or 'drivers', within an organisation which can lead to fair or unfair consumers outcomes. We think using this framework will help us (and the senior management in firms) to understand some of the root causes of unfair consumer outcomes, and therefore reduce the risk that customers are treated unfairly.

We have identified the key cultural drivers to be: leadership; strategy; decision making; controls; recruitment, training and competence; and reward. We believe these drivers are likely to have a significant influence on behaviours of management and staff, and therefore on consumer outcomes.

For each driver we have identified the associated indicators and contra-indicators of good behaviour. The framework will enable supervisors to assess the risk a firm's culture presents to treating customers fairly.

A separate management behaviours framework has been drawn up for the smallest firms who have shorter reporting lines and a simple business model, to identify the key management behaviours which could have an impact on whether a customer is treated fairly (see Annex II). However, for some of the larger or more complex firms supervised by our Small Firms Division, the main culture framework is likely to be more appropriate.

During the development of the frameworks, we have visited a cross-section of 21 firms to check we have identified the correct drivers and make sure the indicators and contra-indicators are appropriate. We have also reviewed past enforcement cases, skilled persons' reports and private warnings to help identify the drivers that gave rise to the identified risk. We have also tested the framework to see if it would have identified crystallised risks in other firms. We have made changes to the culture frameworks that we initially published in May, including a merge of the 'internal communications' driver with 'leadership'.

How we will use the framework

The culture framework applies to retail firms and to wholesale firms where they have retail customers or manufacture products for distribution to retail consumers.

The frameworks are not intended to be a checklist for supervisors or firms of what a good TCF culture should look like. We recognise that firms may well have different cultures yet still treat their customers fairly.

We intend to integrate the culture framework into our ARROW risk assessments, where appropriate. We already look at a firm's culture as part of the ARROW risk assessment and the framework will enable supervisors to assess TCF culture in a more structured and in-depth way. This will include spending more time talking to middle management and frontline staff, where they may have an impact directly, or indirectly, on consumers to see if their behaviours and actions are appropriate and consistent with the values expressed by senior management, and whether these would lead to fair consumer outcomes. This approach is consistent with principles based regulation. We will also conduct culture visits to firms outside of the usual ARROW cycle. We will deliver full training for supervisors on the framework in advance of using it on firm visits.

The letters we send firms after an ARROW risk assessment may include statements about the culture in the firm towards treating its customers fairly if the relationship management team feels there are issues to be raised. As with all risks, risk mitigation programmes may include work to be undertaken by us, or by the firm, on the specific potential or actual risks identified.

If we are satisfied a firm has robust systems and controls and the senior management are reviewing and using reliable MI which demonstrates that they are treating their customers fairly, we will significantly reduce the level of testing we carry out on the firm's culture regarding treating customers fairly.

We will also consider how the culture framework can be used within our thematic reviews to identify the cultural drivers behind a TCF issue that has occurred in a number of firms or across a sector.

Our Small Firms Division will use the findings from our culture work, and the culture frameworks, to help develop engaging tools and messages targeted at small firms.

As with our enforcement work in general, we will consider whether it is appropriate to refer a firm or its senior management to Enforcement where we identify actual or potential consumer detriment.

How firms may use the framework

Senior managers may wish to use either framework to assess the TCF culture within their firm. While the drivers, indicators and contra-indicators can be used as a guide, senior management will need to consider any other issues that may impact on the culture.

4 Leadership

Leadership within a firm includes senior management and any person with responsibility for managing staff. Leaders will have a very significant influence over the TCF culture of a firm, through their values and behaviour. When firms make customers central to their behaviours and values, with adequate monitoring of TCF, they are very likely to deliver fair consumer outcomes.

The effective delivery of key messages to staff on the fair treatment of customers is important in the delivery of fair consumer outcomes.

Management at most levels appear to understand the importance of TCF but many have failed to implement this fully within their firm, or within their business area. From our visits to verify the framework we identified that leadership often presented a risk to treating customers fairly.

Good practice – leadership
• **Demonstrating commitment to treating customers fairly** – In a number of firms, the Chief Executive or senior management demonstrated their commitment to TCF by providing clear TCF messages in presentations (including video broadcasts for staff in remote locations) and appearing in internal website downloads, posters and booklets. These communications explained what TCF meant for the firm, the challenges they faced, and provided regular feedback on their progress. • **Strong TCF leadership** – In one firm, the Chief Executive established two clear TCF-related objectives for all staff. The strategy, policies and procedures were driven by these objectives and supported by clear direction from senior management. This created the right conditions for a good TCF culture to evolve, in both the firm and their outsource partner. • **Maintaining high standards of TCF** – One firm discovered that an ex-adviser had tampered with client records. Although it had been relatively easy to reconstruct the records, the firm had spent considerable time and money pursuing this matter through the courts. The management did this primarily because, among other reasons, they wanted to make it clear to all staff that they would not tolerate any behaviour which was against the interests of their customers. • **Listening to, and acting on, staff feedback** – In two firms, staff could give anonymous feedback to senior management if they believed that their firm was not treating its customers fairly. The senior management could demonstrate that they were giving consideration to this feedback and, when necessary, were prepared to take action.
Poor practice – leadership
• **Failing to identify what TCF means** – In some firms, senior management had failed to identify or articulate what TCF means for the firm, or to discuss what it means for specific areas of the business. Middle management had identified for themselves what they thought TCF meant, but there was no discussion with, or challenge from senior management. • **Inappropriate delegation of TCF** – In a number of firms, senior management established TCF visions and values but delegated the responsibility for implementing these to middle management without adequate direction and monitoring. Where senior management fail to do this, there is a potential risk that the firm applies an incoherent TCF strategy which could lead to unfair consumer outcomes. • **Method of delivering not right for the importance of message** – One firm had a large call centre in a satellite office, but senior management were located in the firm's head office. Head office staff received key messages on treating customers fairly directly from senior management but the call centre were given TCF messages by junior members of each team, after a session with their training department. Where a firm fails to deliver TCF messages consistently and in an appropriate manner there is an increased risk that staff will fail to take the appropriate action. • **Outcomes inconsistent with strategy** – We have seen examples in a few firms where middle management has established a process or procedure which is inconsistent with the TCF strategy adopted by the firm. One firm had a customer charter, which included statements of how the firm would treat customers fairly. However, this was not delivered by staff in customer-facing positions. • **Failure to identify TCF risks and take action** – In one firm, the Chief Executive and Chief Operating Officer had concerns over the capability of a large number of the firm's advisers. In addition, the Compliance Director was sent a report which highlighted potential serious risks with the advice given to customers. However, the Sales Director did not believe there were any problems with his staff. There appeared to be different views on the abilities of the advisers and it was not clear what steps senior management were taking to resolve this or to ensure any necessary action was taken.

5 Strategy

Strategy includes any forward-looking plan developed by senior managers and leaders. This may include change management programmes, the development of significant new products or target markets, or material outsourcing arrangements.

The fair treatment of customers needs to be considered when planning and implementing a strategic change.

Many firms have adopted a strategy that includes treating customers fairly, in line with the visions and values of senior management, but this is often not implemented in a way that encourages the fair treatment of customers.

Good practice – strategy
• **Understanding consumer needs** – One firm invited a number of consumer bodies, including Which?, National Consumers Council and Citizen's Advice Bureau, to help it develop its retail products and services, including its approach to TCF. • **Valuing customer feedback** – A number of firms identified the importance that customer feedback can play in developing their strategy, products and services. They introduced formal customer feedback procedures, including customer forums, to help them formulate their products and services. They also used customer feedback forums to test their approach to particular issues. For example, one firm asked the forum to give them their views on how the firm should respond to complainants. • **Choosing a third party with consistent TCF values** – One firm outsourced the administration of its funds to a third party. It chose a firm that had TCF values which were aligned to its own and monitored the delivery of its TCF objectives by placing staff in the outsourced firm. • **Clear and consistent strategy** – In developing their strategy, one firm had taken account of the six TCF outcomes. This strategy had been translated into simple language which would be easily understood and remembered by staff. In our discussions with staff, they referred to the message and could demonstrate how this applied to their day-to-day activities.
Poor practice – strategy
• **Failing to identify the impact strategy may have on TCF** – In one large firm which had embarked on a strategy to grow the business, the Compliance and Operations Directors saw a significant increase in their workload and a need to be away from their office for long periods of time. The firm did not appear to have considered fully the impact that their strategy would have on their senior and middle managers' ability to monitor existing business and, in particular, the fair treatment of their customers. Since the visit, the parent firm has completed an operational risk review and, as a result, the resource issue has been acknowledged and is being addressed. • **Outcomes inconsistent with the TCF strategy** – One large firm had a clearly defined TCF strategy, which was set out in the firm's TCF values and was driven by senior management. However, shortly after embarking on this strategy they acquired more business. The senior management reduced the amount of resource allocated to TCF, resulting in a delay in embedding TCF within their culture. Any decision by a firm to relax or suspend their approach to treating customers fairly could give an impression that they are not committed to TCF. • **Lack of senior management oversight** – In one small firm, two principal directors had outstanding personal issues with a previous employer and faced a legal challenge. They also needed to make sales for their new firm to maintain a high level of income. As a result they did not allocate enough time to controlling and overseeing the firm's advisers, of which five were not appropriately qualified. In this case, the personal needs of the directors led to significant risks for their customers and resulted in unfair consumer outcomes. • **Delegating TCF responsibilities to a third party without monitoring the outcomes** – In a number of firms, we have seen outsource arrangements where the third party is not required to demonstrate they treat customers fairly and/or they are not monitored against delivery of fair consumer outcomes. Where firms employ the services of a third party they still have the responsibility to deliver, and monitor, fair consumer outcomes. • **Inappropriate reliance on TCF strategy** – A number of firms felt that simply referring to their strategy demonstrated they were delivering fair consumer outcomes. This included relying on statements rather than evidence to suggest they would not mis-sell or that customers would understand their products clearly. For example, 'we only offer simple products', 'the product is suitable for all our customers' and 'we get referrals from customers and very few complaints'. In these examples the firms have not gone far enough in understanding the risks to consumers, or in monitoring outcomes.

6 Decision Making

Decision making at all levels gives an indication of the TCF culture within a firm. It refers to any situation where an individual is expected to make a decision that could have an impact, directly or indirectly, on delivery of fair consumer outcomes.

When making a decision, the interests of one group of customers should be properly balanced against other groups of customers and shareholders.

We have identified a significant number of instances where the decisions that have been made have not reflected fair consumer outcomes.

Good practice – decision making
• **Making a difficult decision in order to demonstrate TCF** – Two firms, despite already committing considerable resources, decided not to proceed with products they had developed. In one case, a firm felt their product posed too great a risk to customers. The other firm, after further testing with customers, decided the benefits of the product were not enough for their target audience. In these examples the firm had taken a difficult decision in the interests of their customers. • **Making the right decision** – One firm took over the management of a particular fund from another firm. A few years later they identified, due to the volatility in the investment market for this type of fund, that many customers may not have realised the risks associated with this type of investment. The firm decided to contact all customers[6] with investments in this fund to make them aware of the risks and to suggest they seek advice. In this case the firm decided contacting the customer was the right approach, even though they could incur substantial costs. • **Integrating TCF within business process** – A couple of firms introduced a formal process for considering TCF within their product design and financial promotion procedures. Decisions were also clearly documented including consideration of the relevant TCF factors, the rationale behind any decision, any actions required and who had made the decision.
Poor practice – decision making
• **Failing to challenge a process** – In a number of firms, the effectiveness of processes and technology was questioned by customers but their concerns were not adequately investigated. Front-line staff failed to challenge inappropriate guidance and procedures provided by senior and middle management. In one firm, the branch policy was to give customers information not advice and the complaint handlers rejected, on principle, any suggestion from a customer that they received advice. In another firm, the IT systems were considered perfect and call centre staff did not accept, or register, any customer complaint over access to the system or queries over the transactions recorded. In these examples, the firms did not appear to investigate fully the concerns of the customer, which may have called into question the guidance staff had been given. • **Ability to make a decision** – A claims handler at one firm was responsible for dealing with a particular type of claim. However, he always checked his draft decisions with his manager, as he was uncomfortable about making decisions on these claims unaided. This was despite the fact he had formal authority to make decisions on these claims without reference. This raised concerns with his ability to apply his authority limit confidently when his manager is unavailable, which could result in unfair decisions for customers. Under these circumstances, we would question whether this individual should have had this authority. • **Failing to record the basis of material decisions** – A number of firms failed to record, and so could not justify, why the senior management took a particular approach. For example, why a firm had decided that a complaint trend did not have a wider impact. • **Failing to identify risk** – In one advisory firm, a Compliance Director asked a third party to review a large number of client files to check for suitability of advice. The result was a very high failure rate. However, he did not appear to recognise the significance of this finding and did not consider the risk of mis-selling as he assumed the high failure rate was due to poor record keeping. • **Potentially misleading approach to customers** – We identified a number of examples where the job title of the individual, or the approach being made by the firm, may have given the customer the wrong impression over the reason for the firm's contact with them. In these situations, the customer may not have realised the firm was making a sales approach. • **Inappropriate decision in complaint handling** – In many firms, we have identified unfair outcomes for consumers through poor decision making by complaint handlers. Complaint handling can be a good indicator of a firm's inclination to be fair and objective in its dealings with customers. This is evident not only through complaint handling itself, but also through analysing the root cause to identify improvements in processes and controls, and the willingness to undertake wider reviews where unfair consumer outcomes have been identified.

6 A firm may wish to consider contacting its PI insurer before contacting its customers. However, this does not remove its obligation to treat its customers fairly.

7 Controls

Controls, including MI, are a key part of a firm's risk framework and enable a firm to manage their customer risks and to identify poor performance. Appropriate MI needs to be available to all levels of management to demonstrate that the customer risks they are responsible for are being managed appropriately and that they are delivering fair consumer outcomes.

Customer feedback can provide valuable information on the effectiveness of controls and the delivery of fair outcomes for consumers.

Controls, including MI, are important to the delivery of a good TCF culture. However, we acknowledge that for many firms TCF MI is proving to be a significant challenge.

Good practice – controls
• **Checking staff understand and implement TCF** - One firm completes quarterly 'knowledge health checks' in the form of 30-minute interviews with randomly selected members of staff to check they understand and apply key issues correctly. A report is produced for senior management and middle management, which summarises the interviews and suggests corrective action where a weakness in the approach has been identified. This shows the firm checks understanding and implementation and considers this to be useful MI to support delivery of fair consumer outcomes. • **Monitoring delivery of fair consumer outcomes** – In one firm, all members of the management team from CEO to Team Leaders listen to two hours of randomly selected call centre calls. They then give the staff involved immediate constructive feedback. This is a useful control and the information gathered could be used to show the firm is checking consumer outcomes and correcting poor behaviour. • **Checking TCF behaviour and feedback** – One firm used a hidden camera 'mystery shopping' exercise to monitor front-line staff and to identify examples of good and bad practice. Staff watched the results online or on DVD which included an accompanying commentary by senior management. The 'learning' points identified during this exercise and the process for feeding this back to staff appeared effective in influencing staff.
Poor practice – controls
• **Confusing the customer** – In many firms, controls are focused on delivering information but do not give enough consideration to customer understanding. In one firm, we identified a strong controls culture, which ensured that call centre staff provided the customer with all the facts about a product. But in one call, a very large amount of this information was simply read out without any break, and it was clear that the customer had 'switched off' during the conversation. Where a firm discloses a lot of important information over the phone, it may wish to consider ways it could retain the customer's attention throughout the conversation. • **Limited qualitative data** – We have identified that firms' MI is often limited to quantitative data, which is sometimes very narrow in scope, and is often not supported with qualitative data. In a number of firms, we have seen MI on the products being sold and the commission received, but minimal information on the quality of the sale made. Firms might wish to consider how best to monitor the quality of sales. Appropriate measures vary. In an advised environment, it might be relevant to look at incidence of advice without a (commission earning) product sale, as well as execution only or insistent customer business. For products with high upfront costs, persistency is of interest. Data on refused claims or complaints can also be informative. This will enable a firm to monitor the competence of the adviser and the quality of their sales. This information could also be reflected in the assessment of the competence of the adviser. It may also be useful in reaching a conclusion over the validity of a customer complaint as part of any investigation where the suitability of the advice is being questioned. • **Ineffective controls** – We have identified ineffective controls in some firms. One firm monitored the number of investment trades to identify potential 'churning'. However, the firm did not use this information to investigate potentially poor sales, but instead it wrote to the client to ask if they were satisfied with the advice. This is not enough evidence on the quality of the sale as the client may not realise that they have been subject to 'churning'. It is important where MI is collected that appropriate action is taken to ensure that the risks to consumers are minimised. • **Not enough focus by senior management** – One firm had structured their TCF programme around their processes and delegated responsibility for their action plans to managers owning the processes. A significant amount of activity had taken place but the resulting MI was not focused enough to enable senior management to monitor progress and explain if the actions mitigate their key TCF risks. For example, the CEO could not tell how the firm would factor TCF into key decisions, or whether they had made any progress in two significant areas for the firm. The firm has now re-started a 'top down' gap analysis, with each key risk and action plan owned by a senior executive. • **Not enough MI** – A number of firms have failed adequately to monitor their advisers. They did not collect data on the number of instances, either on an individual or group basis, where they were delivering unfair consumer outcomes. One firm did not take corrective action when this occurred. • **Failing to collect MI** – One firm had not developed controls to capture and monitor customer feedback received by the call centre. This meant the firm was unable to identify where they had failed to meet their own internal service standards, or how it could be improved.

8 Recruitment, training and competence

A firm can influence the delivery of fair consumer outcomes by recruiting staff with appropriate values and skills, training staff effectively, and assessing and monitoring their competence.

A robust performance management framework with clear and appropriate objectives linked to the fair treatment of consumers, which are regularly reviewed and acted on, will support the delivery of fair consumer outcomes.

Most firms have yet to consider how their objectives can best reflect the fair treatment of customers within their performance management plans, or how they can monitor the competence of the individual in delivering fair consumer outcomes.

Good practice – recruitment, training and competence
• **Meeting recruitment needs** – One firm had a strong business need to recruit a new adviser. Although they had advertised the post nationally, they had not found anyone within the financial services industry who they felt would fully align themselves with the firm's vision and values. So the firm invested considerable time and resource to train someone new to the financial services industry, who they felt would have the requisite TCF behaviours. • **Learning from experience** – One firm undertook a monthly root cause analysis of complaints with useful commentary on the reasons why customers had complained. This analysis was widely circulated within the firm and the firm planned to use additional commentary on good practice to avoid similar complaints in future. • **Consistent objectives** – We have only identified one firm during our visits where the TCF-related objectives of the Chief Executive, senior and middle management, front-line staff and outsourced partners are fully aligned. • **Recruiting the right people** – In growing their business, one firm agreed to takeover the salesforce of another firm. The firm insisted all 212 experienced advisers went through the standard recruitment process and in-house training programme. As a result, the firm employed only 140 of the 212 advisers. This firm ensured that all new staff, regardless of their previous sales experience, had similar TCF values to their own.
Poor practice – recruitment, training and competence
• **Lack of, or unclear TCF objectives** – In several firms, objectives for staff, at many different levels, simply included an objective 'to treat their customers fairly' with no guidance on the behaviours or actions needed to meet the objective. In addition, some firms did not appear to have objectives that would deliver fair consumer outcomes. • **Failure to correct poor performance** – In two firms, we identified that senior management were aware that middle management were potentially delivering unfair consumer outcomes. However, the senior managers had not challenged the middle management and had not taken appropriate action to improve their performance, or to remove them from the firm. • **Failing to measure and monitor TCF behaviours** – One firm developed a clear strategy to ensure that all staff had a simple and clear definition of how customers should be treated. The senior management team delivered appropriate training, with posters, brochures and internal website links, describing the behaviours they wanted staff to demonstrate. However, it was not clear whether the behaviours had been included within individuals' objectives or how they would measure and monitor these. Firms may wish to consider how best they can measure and monitor staff performance in delivering fair consumer outcomes, including appropriate measures in performance management plans, where relevant. • **Failing to identify training needs** – In one firm, staff were left to decide for themselves what training and development they might require with very little direction from management on what might be useful from a personal development or business perspective. • **Failing to monitor performance** – One firm recruited an adviser who was new to the financial services industry. The adviser's performance was monitored in a very informal manner and the firm was not proactive about giving feedback. It was left to colleagues to point out anything they overheard the adviser saying on the phone, or in face-to-face discussions with customers. As part of the training programme the adviser only had to undertake two role plays before he progressed to selling more complicated products and was not subjected to any ongoing monitoring.

9 Reward

A reward strategy includes a number of aspects, such as salary, bonus and commission, as well as profit sharing, and staff incentive and recognition schemes.

We recognise the need for firms to establish targets, where appropriate, which will lead to growth in the business and sustainable and increasing profits. We also acknowledge that firms can motivate their staff to deliver this through rewarding performance and recognising success. However, controls play a key part in preventing unfair consumer outcomes, at all levels in the business, including monitoring of individuals.

We recognise that existing contractual arrangements with staff may make it difficult to change the reward structure. In these cases, firms may wish to consider what safeguards they can introduce to mitigate any risks the reward structure may pose to fair consumer outcomes.

From our visits, we identified that some firms have failed to recognise the influence of incentive schemes on delivering unfair consumer outcomes. Where firms have reviewed their reward structures, they have often not put sufficient weight on quality issues and do not go far enough in rewarding good behaviour or fair consumer outcomes.

Good practice – reward

- **Reward as a TCF incentive** – In one firm, all staff, including the sales-force, were remunerated through salary and a share options scheme. No commissions or bonuses were paid. Building customer loyalty, including further sales through an emphasis on customer service, was a key objective in this firm. Staff were incentivised to act in the long term interests of the firm by treating their customers fairly.
- **Recovering inappropriate commission** – Many firms have arrangements in place so that regular commission payments are not made until an independent check of the client file has been made. Commission is 'clawed back' where the client has surrendered the product or where a complaint about the sale has been upheld. Some firms have already extended, or plan to extend, this clawback arrangement to the managers of the sales force where they receive a percentage of the commission payments generated by their staff.
- **Rewarding quality** – Other firms took a different approach and paid a yearly bonus to advisers based on sales targets. They withdrew or cut back the bonus if quality objectives were not met. But, the management of these firms stressed that quality issues were constantly fed back to advisers and so cutting back on bonus would be seen as a failure of the other procedures they used to maintain quality.
- **Recognising good TCF behaviours** – A number of firms had recognition schemes for staff that had excelled at good customer service, including TCF. These included awards presented by senior management and spot bonuses. One firm introduced a 'rewarding excellence' incentive scheme. This scheme rewarded individuals who could give practical examples of how they had incorporated the firm's TCF behaviours in their day-to-day activity.

Poor practice – reward

- **Rewarding inappropriate behaviour** – In two firms, the senior management teams were set challenging targets by their parent company based on return of capital, growth and cost reduction. Their reward package was based on achieving these targets with failure or challenge being met with disciplinary action. As a result, the decisions taken by senior management were heavily focused on meeting their targets, without any consideration to quality. We also noted the firm had a high turnover in its senior management team and had difficulty in filling senior management vacancies.
- **Ineffective TCF incentives** – In a number of firms, it was not clear what targets and objectives were set for senior management, and where they did exist they often referred to profit, income or growth. Where senior management objectives did reflect fair consumer outcomes, either directly or indirectly, the weighting given to these objectives often appeared lower than others, for example, making sales, driving up income or reducing costs. Therefore any negative impact on the individual's reward for failing to meet a TCF objective was potentially more than compensated for by delivery of other targets. To deliver consistently fair consumer outcomes, firms may also need TCF-related objectives (with appropriate weight) for their senior management, with failure to meet these having a clearly defined impact on their individual reward.
- **Insufficient TCF objectives** – In one firm, senior management performance scorecards had insufficient indicators of TCF performance. The firm identified 'no major FSA concerns' and 'no major regulatory sanctions threatened' as the only indicators that senior managers had met their target. In isolation, these indicators are not an effective test of TCF behaviour and do not encourage the dynamic behaviour necessary to achieve fair consumer outcomes.
- **Inappropriate recognition** – One firm did not have appropriate controls around promotion. An individual was promoted as a direct result of the amount of business and the level of income generated for the firm, and we could not identify if quality checks had been completed before the promotion was approved. In addition, this firm did not have appropriate controls or MI on the advice given and there was limited senior management oversight. Promoting an individual within a firm, based solely on income achieved without any consideration of the quality, may encourage individuals to increase income without adequate consideration of treating their customers fairly.
- **Inappropriate incentive schemes** – In one firm, the directors received a salary based on a percentage of the income their department achieved and bonuses for income achieved in excess of their target and for undertaking additional duties. We were concerned this could lead to unfair consumer outcomes due to the focus on generating income without any consideration to the quality of the business.
- **Failure to take timely action** – Although we have issued past TCF publications on remuneration, in particular the cluster reports, we saw firms where the current reward structure was still based on sales with no recognition of quality measures. In a couple of firms, while plans were in place to change these reward structures in 2008, only limited interim quality measures were established for this year.

Annex 1

Culture framework

Key drivers and high level indicators and contra-indicators

Indicators	Key Driver	Contra-indicators
Fair treatment of customers is central to the behaviour and values of all managers, they communicate messages about the fair treatment of customers effectively and apply appropriate controls and monitoring to ensure that the fair treatment of customers is delivered by their staff	**Leadership**	Managers (at any level) cannot explain and/or do not communicate what the fair treatment of customers means for them and their staff and cannot demonstrate that their staff understand what the fair treatment of customers means
The firm has a clear vision which supports the fair treatment of customers. This is reflected within the formulation and implementation of strategic decisions (including change management programmes and outsource arrangements). The firm's risk appetite reflects customer considerations	**Strategy**	The firm's vision is unclear/blurred or contradicts the fair treatment of customers. It does not consider the fair treatment of customers when making key decisions about future direction
Decision making at all levels reflects the fair treatment of customers. The firm uses staff, customer and other external feedback where appropriate, with timely action. The interests of customers are properly balanced against those of shareholders (and other customer groups)	**Decision making**	Minimal evidence that decisions reflect any consideration of the impact on customers. The firm is slow or unwilling to react to customer/staff feedback. Conflicts between the interests of shareholders and customers are consistently and inappropriately resolved in favour of shareholders.
The firm has controls, including management information, that aim to ensure and demonstrate the fair treatment of customers. These controls are integral to the firm's risk framework	**Controls**	The firm cannot evidence customer protection through its controls, has minimal management information and does not use this information to improve its treatment of customers
Management make positive behaviours and attitudes to the fair treatment of customers a key criterion in the selection of staff. They also make effective training and the maintenance of staff knowledge, behaviours and values core to the business. Managers use performance management to develop their staff in the fair treatment of customers, identifying and acting on poor performance and rewarding good performance	**Recruitment, training and competence**	The firm has inadequate arrangements to recruit, train and assess the competence of staff whose actions affect customers. It has little focus on the fair treatment of customers and has a lack of appreciation of how staff competence has an impact on customer experiences. Poor performance is tolerated
The firm's reward framework (including incentive schemes) throughout the business is transparent, recognises quality and supports the fair treatment of customers	**Reward**	The firm's reward framework concentrates on sales, volumes and profit without consideration of quality (i.e. the framework drives behaviours which may result in customers being treated unfairly) and there are no controls that mitigate the risks that arise from this framework

Leadership* - indicators and contra-indicators

Indicators	Leadership	Contra-indicators
Managers have established and can explain values which reflect the fair treatment of customers. Their behaviours support these values. They are supportive of staff	**Core values**	Managers put personal considerations above all others. They cannot explain what fair treatment of customers means for them or their staff
Managers lead by example, by being honest, fair and inspiring staff to treat customers fairly	**Acting with integrity**	Managers display behaviour that you would not expect of a person in their position e.g. untrustworthy, indiscreet, etc.
When management set plans and priorities they are consistent with the firm's vision and values. They give the fair treatment of customers appropriate prominence and resource relative to other business needs. Management undertake monitoring to ensure that actions on the fair treatment of customers agreed at the planning stage are delivered	**Planning and execution**	Management do not identify, give low priority or inadequately consider the fair treatment of customers. No check is made that the planned actions to help the fair treatment of customers are being delivered
Managers communicate clearly, and at the right time, on issues that have a material impact on the fair treatment of customers. They correctly identify to whom the message needs to be directed and use an appropriate format at the right time. They check that the message has been understood and acted on	**Communication**	Managers take a 'scatter gun' approach to direct messages, on the fair treatment of customers, which are not tailored to suit their intended audience. There is little demonstration that messages are understood or acted on
Managers actively develop the competence of their staff whose actions affect customers and ensure the development of a strong learning and support culture, empowering individuals to take accountability for the delivery of the fair treatment of customers	**People development**	Managers take no interest in staff development and are unconcerned about the impact incompetent staff will have on the customer
Managers have a strong understanding of the risks to customers within their operation and how these will be mitigated. They are open to challenge, and will challenge their own managers, on issues that affect the fair treatment of customers	**Operational excellence**	Managers have little understanding of the organisation, its operation, or how these impact on the customer. There is no mechanism for staff to challenge issues that affect customers or the environment is not conducive to challenge

* Leadership within a firm includes senior management and any person with responsibility for managing staff. These people are referred to as 'Managers' in this table

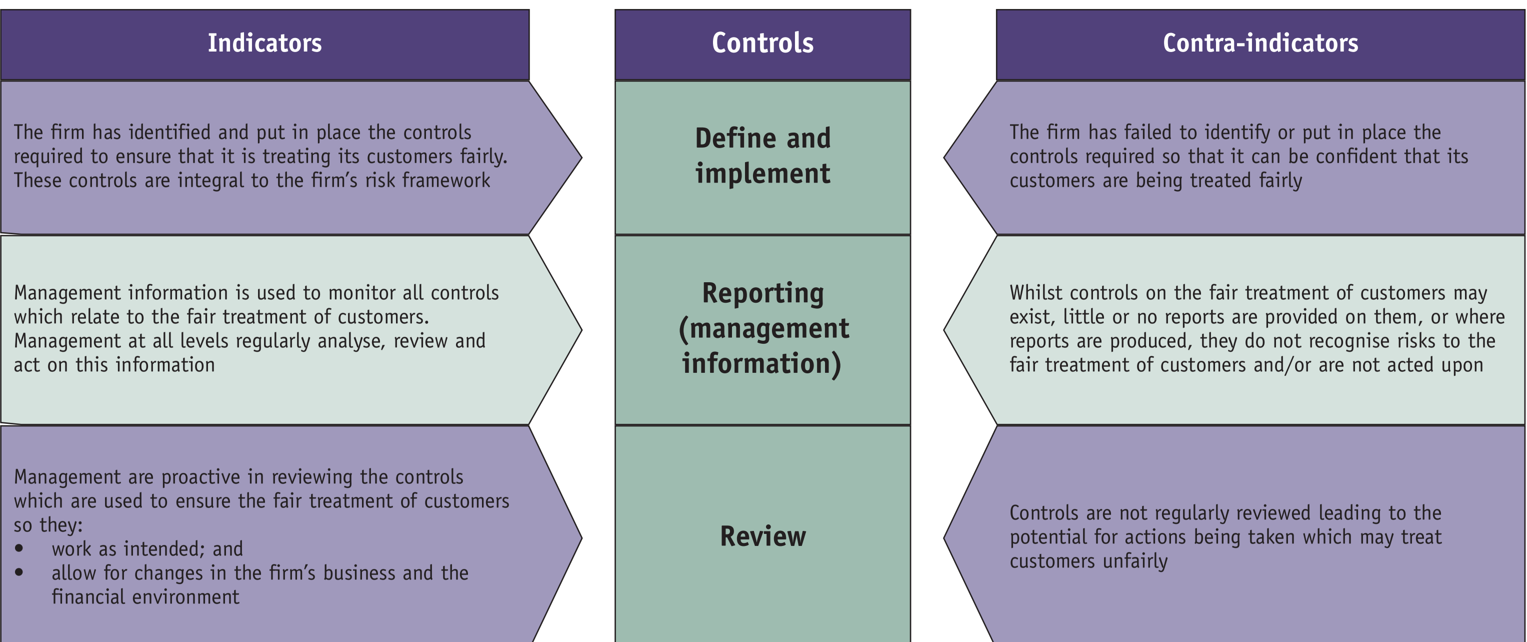
Strategy – indicators and contra-indicators

Indicators	Strategy	Contra-indicators
The firm's vision and values are aligned with treating customers fairly. The fair treatment of customers is reflected in a clearly defined and realistic strategy. When the firm develops, or amends, and implements the strategic plan (including change management programmes) the firm aligns this with the fair treatment of customers	**Strategic perspective**	A strategy has been implemented, or an existing strategy changed, without consideration of the impact on the customer
The firm uses customer surveys, research and other external feedback (such as complaints and feedback from consumer bodies) to assist in the development of strategy. It updates the strategy to reflect changing customer needs as well the external environment. The firm's risk appetite reflects the fair treatment of customers	**Consumer perspective**	The firm does not seek external feedback or use the feedback that comes to it
Management put the necessary resource - financial, staff and systems - in place at the right time to deliver the strategy (which helps customers to be treated fairly)	**Resource**	There is little or no recognition of the resource required to deliver the strategy, or the required resource is late. No checks are made that the resource remains adequate
Management develop people, technology, policies and procedures in line with the needs of the strategy, delivering products and services consistent with the business and treating customers fairly	**Development of the organisation**	The strategy is being developed without a complementary development of staff, technology, policies or procedures necessary to ensure the fair treatment of customers

Decision making - indicators and contra-indicators

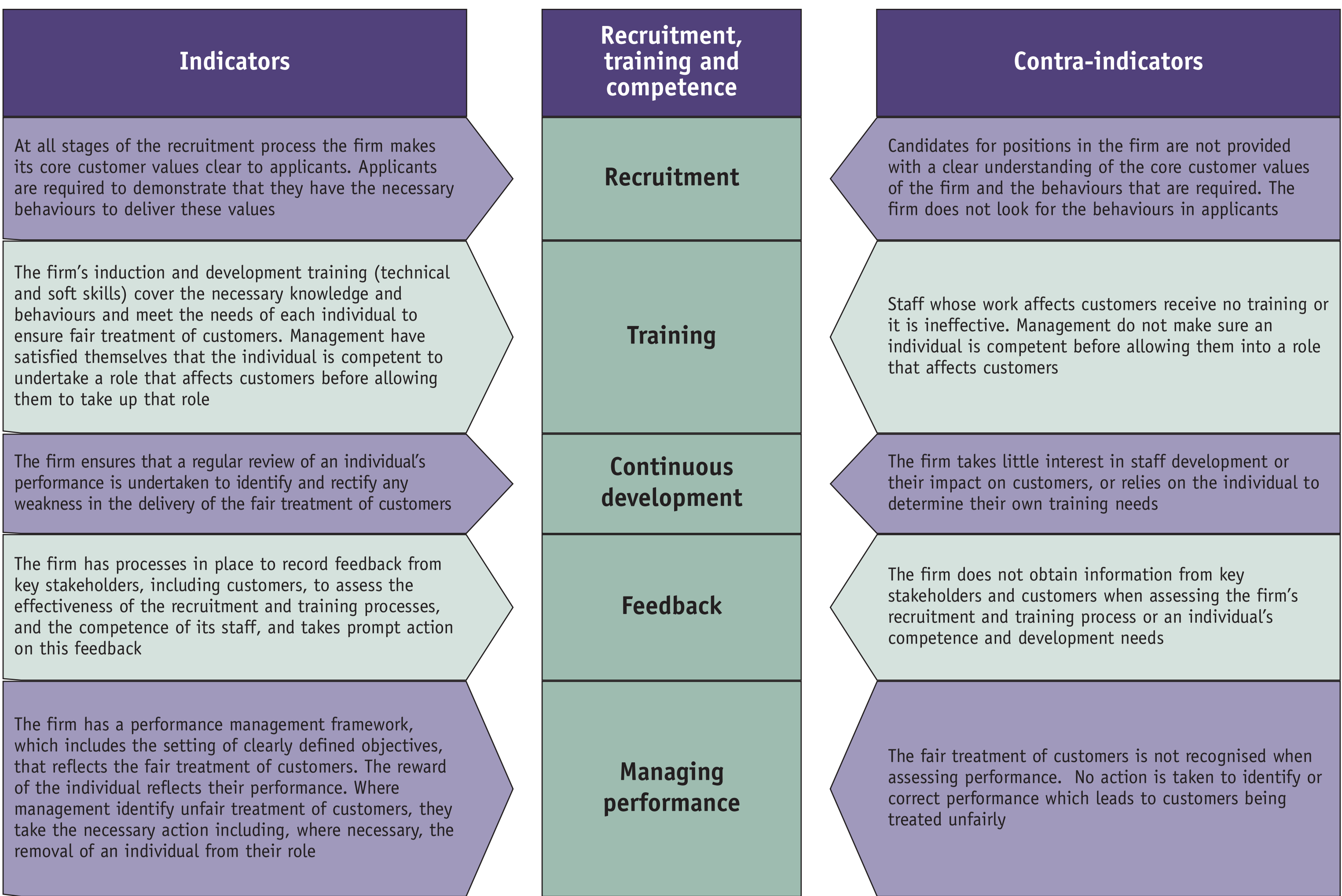
Indicators	Decision making	Contra-indicators
Where decisions are taken that affect customers, the decision maker always gathers the relevant information. This includes feedback from customers and staff where this will help ensure a fair outcome for customers	**Informed**	Unfair decisions are taken because insufficient information has been gathered. Decision makers do not consider or investigate relevant feedback from staff or customers
Individuals have the relevant skills and expertise to enable them to take a decision that affects customers. Where they recognise they do not have sufficient understanding, they have access to expert guidance. They understand the need for decisions to take account of the interests of different customer groups and shareholders	**Competent**	Decision makers lack the necessary skills or expertise and are unwilling or unable to seek advice. They generally favour shareholders' interests over those of the customer
Individuals have the confidence and authority to take the decisions required of their role and understand when they need to escalate the decision. This includes circumstances where a flexible approach provides a fairer result for a customer	**Empowered**	Individuals lack confidence or misunderstand their authority leading them to make unfair decisions (e.g. a failure to recognise an individual customer's circumstances) or to be indecisive
Management have created a culture where staff can challenge decisions made about customer issues. The firm recognises challenge from customers and acts on this when it is fair to do so	**Open to challenge**	Staff do not feel they can challenge decisions which they think are not fair to customers. There are inadequate mechanisms to allow challenges from customers. Challenges from customers are dismissed without consideration
The firm records decisions about customer issues including the rationale for what was decided. It maintains these for an appropriate length of time. The records can be accessed easily when required	**Recorded**	There are poor or incomplete records of decisions about customer issues which cannot be retrieved easily, or at all

Controls – indicators and contra-indicators



Indicators	Controls	Contra-indicators
The firm has identified and put in place the controls required to ensure that it is treating its customers fairly. These controls are integral to the firm's risk framework	**Define and implement**	The firm has failed to identify or put in place the controls required so that it can be confident that its customers are being treated fairly
Management information is used to monitor all controls which relate to the fair treatment of customers. Management at all levels regularly analyse, review and act on this information	**Reporting (management information)**	Whilst controls on the fair treatment of customers may exist, little or no reports are provided on them, or where reports are produced, they do not recognise risks to the fair treatment of customers and/or are not acted upon
Management are proactive in reviewing the controls which are used to ensure the fair treatment of customers so they: • work as intended; and • allow for changes in the firm's business and the financial environment	**Review**	Controls are not regularly reviewed leading to the potential for actions being taken which may treat customers unfairly

Recruitment, training and competence - indicators and contra-indicators

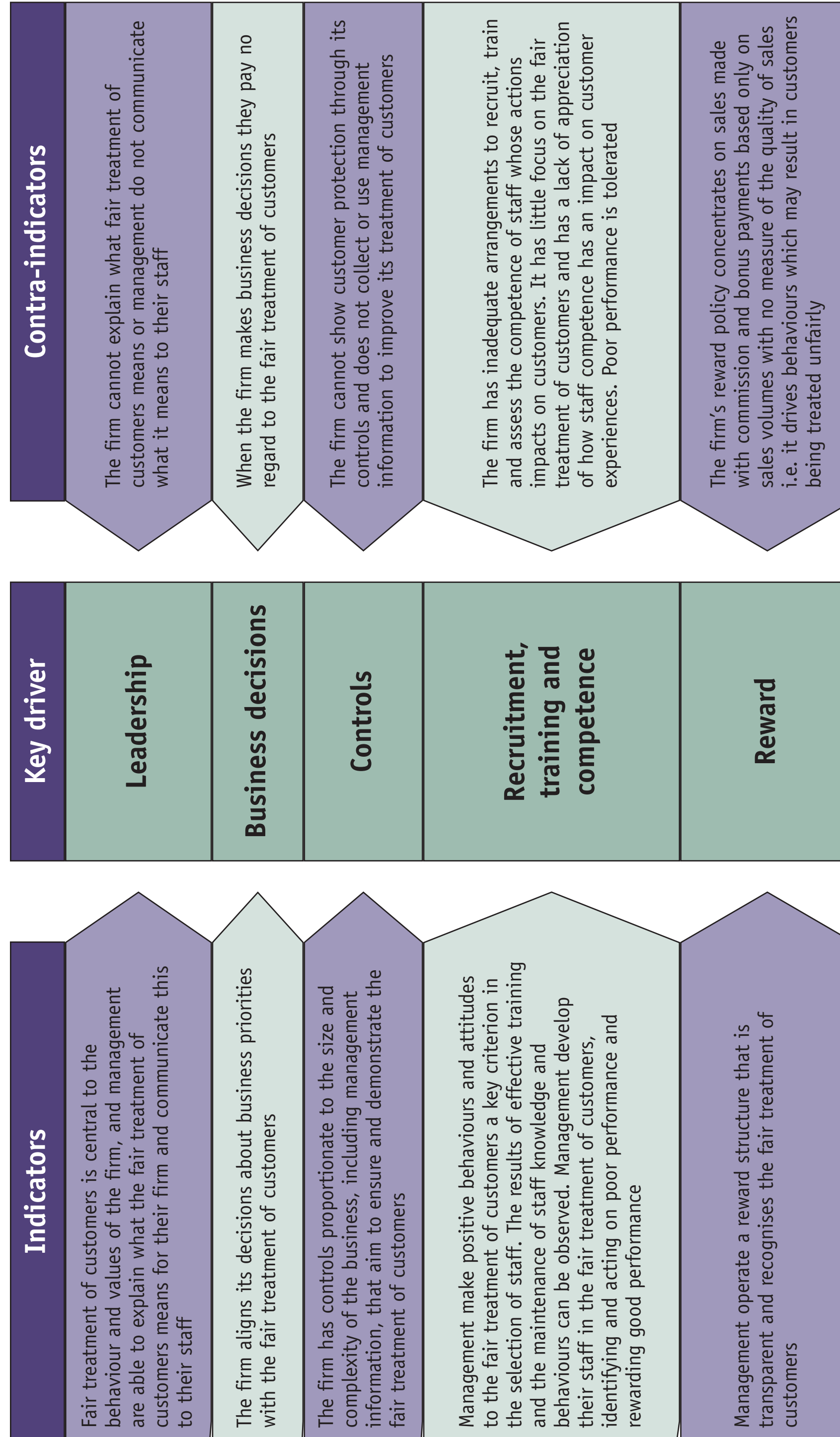


Indicators	Recruitment, training and competence	Contra-indicators
At all stages of the recruitment process the firm makes its core customer values clear to applicants. Applicants are required to demonstrate that they have the necessary behaviours to deliver these values	Recruitment	Candidates for positions in the firm are not provided with a clear understanding of the core customer values of the firm and the behaviours that are required. The firm does not look for the behaviours in applicants
The firm's induction and development training (technical and soft skills) cover the necessary knowledge and behaviours and meet the needs of each individual to ensure fair treatment of customers. Management have satisfied themselves that the individual is competent to undertake a role that affects customers before allowing them to take up that role	Training	Staff whose work affects customers receive no training or it is ineffective. Management do not make sure an individual is competent before allowing them into a role that affects customers
The firm ensures that a regular review of an individual's performance is undertaken to identify and rectify any weakness in the delivery of the fair treatment of customers	Continuous development	The firm takes little interest in staff development or their impact on customers, or relies on the individual to determine their own training needs
The firm has processes in place to record feedback from key stakeholders, including customers, to assess the effectiveness of the recruitment and training processes, and the competence of its staff, and takes prompt action on this feedback	Feedback	The firm does not obtain information from key stakeholders and customers when assessing the firm's recruitment and training process or an individual's competence and development needs
The firm has a performance management framework, which includes the setting of clearly defined objectives, that reflects the fair treatment of customers. The reward of the individual reflects their performance. Where management identify unfair treatment of customers, they take the necessary action including, where necessary, the removal of an individual from their role	Managing performance	The fair treatment of customers is not recognised when assessing performance. No action is taken to identify or correct performance which leads to customers being treated unfairly

Reward – indicators and contra-indicators

Indicators	Reward	Contra-indicators
The firm has performance related salary for staff which recognises the quality of their interaction with customers and the outcomes they deliver. Management make the structure transparent to all employees	**Salary**	Salary is heavily affected by sales or volumes without consideration of quality. Performance development plans incentivise staff to give inadequate service to customers or create the risk of unfair treatment of customers (e.g. encourages staff to pursue quantity at the expense of quality)
When setting commission levels, management recognise qualitative issues such as persistency and complaints. Some recommendations made by advisers do not generate commission	**Commission**	Advisers only have sales and product targets, with few or no quality indicators. Commission is paid up-front without any clawback for inappropriate sales
The firm makes the bonus and profit share framework transparent for all staff and the level of reward takes account of the fair treatment of customers	**Bonus and profit share arrangements**	The level of reward is calculated solely on the extent of income generated and/or growth, disregards the fair treatment of customers and/or is not transparent
The firm treats all staff fairly and understands the impact both formal and informal recognition has on staff. The firm's success measures, including consideration for promotion, recognise the importance of the fair treatment of customers	**Recognition**	Management give informal or formal recognition, including promotion, to employees that excel in making profit or sales without consideration of the fair treatment of customers. These actions encourage other employees to act in the same way

Culture – management behaviours framework for smaller firms



Key drivers and high level indicators and contra-indicators for smaller firms

Indicators	Key driver	Contra-indicators
Fair treatment of customers is central to the behaviour and values of the firm, and management are able to explain what the fair treatment of customers means for their firm and communicate this to their staff	Leadership	The firm cannot explain what fair treatment of customers means or management do not communicate what it means to their staff
The firm aligns its decisions about business priorities with the fair treatment of customers	Business decisions	When the firm makes business decisions they pay no regard to the fair treatment of customers
The firm has controls proportionate to the size and complexity of the business, including management information, that aim to ensure and demonstrate the fair treatment of customers	Controls	The firm cannot show customer protection through its controls and does not collect or use management information to improve its treatment of customers
Management make positive behaviours and attitudes to the fair treatment of customers a key criterion in the selection of staff. The results of effective training and the maintenance of staff knowledge and behaviours can be observed. Management develop their staff in the fair treatment of customers, identifying and acting on poor performance and rewarding good performance	Recruitment, training and competence	The firm has inadequate arrangements to recruit, train and assess the competence of staff whose actions impacts on customers. It has little focus on the fair treatment of customers and has a lack of appreciation of how staff competence has an impact on customer experiences. Poor performance is tolerated
Management operate a reward structure that is transparent and recognises the fair treatment of customers	Reward	The firm's reward policy concentrates on sales made with commission and bonus payments based only on sales volumes with no measure of the quality of sales i.e. it drives behaviours which may result in customers being treated unfairly

Leadership* – indicators and contra-indicators for smaller firms

Indicators	Leadership	Contra-indicators
Managers believe in the fair treatment of customers and their behaviours and values support this. They communicate issues that affect customers clearly, and they are supportive of staff	**Core values**	Managers put personal considerations above all others. They cannot articulate what the fair treatment of customers means for the firm or communicate issues that affect customers poorly or not at all
Managers lead by example, by being honest, fair and inspiring staff to treat customers fairly	**Acting with integrity**	Managers displays behaviour that you would not expect of a person in their position e.g. untrustworthy, indiscreet, etc.
When considering future business changes, the firm gives appropriate priority to the fair treatment of customers	**Planning**	The firm gives no consideration to the fair treatment of customers when considering changes to their business
Managers take a strong interest in the competence of staff and develop an effective learning and support culture	**People development**	Managers take no interest in staff development or are unconcerned about the impact incompetent staff will have on customers
Managers have a strong understanding of the risks to the fair treatment of customers and how these will be mitigated. They are open to challenge on issues that affect the fair treatment of customers	**Operational awareness**	Managers have little understanding of how the firm's operations affect customers or they are unwilling to change their view on issues about the fair treatment of customers

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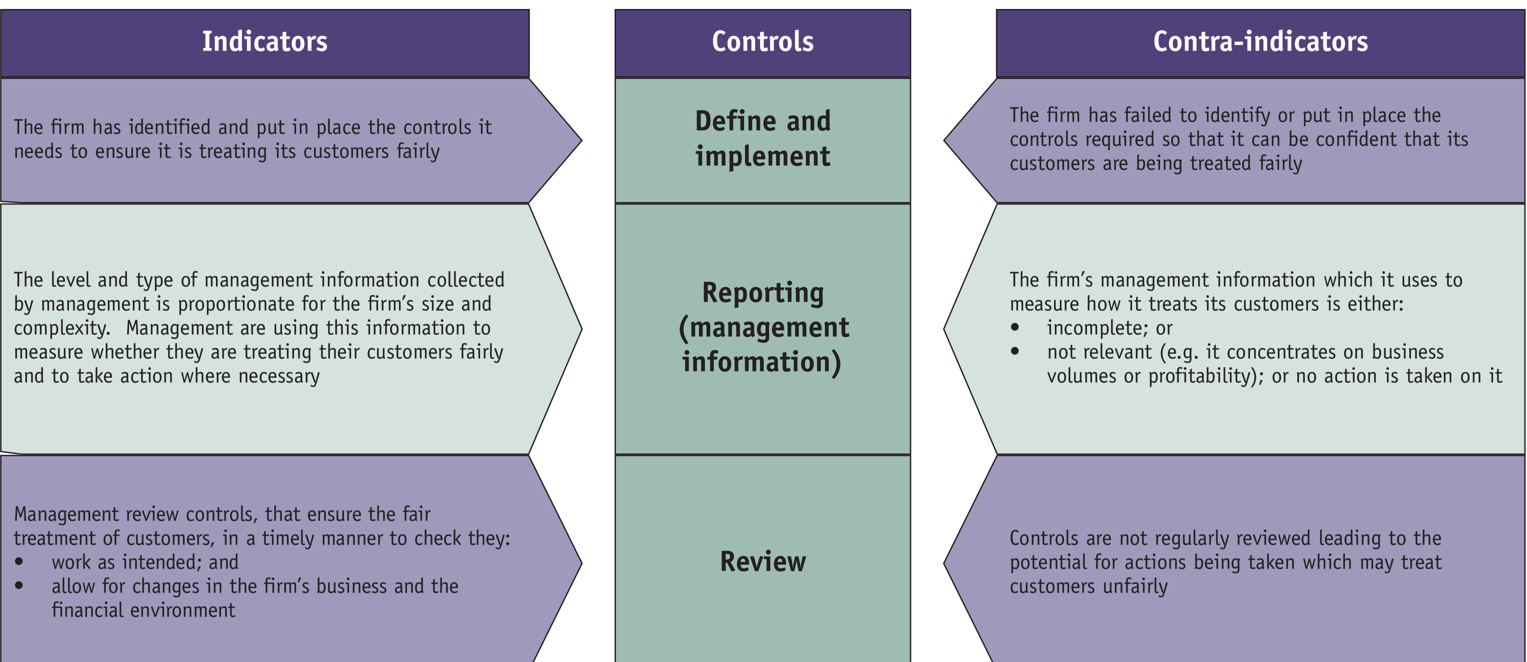
Business decisions - indicators and contra-indicators for smaller firms

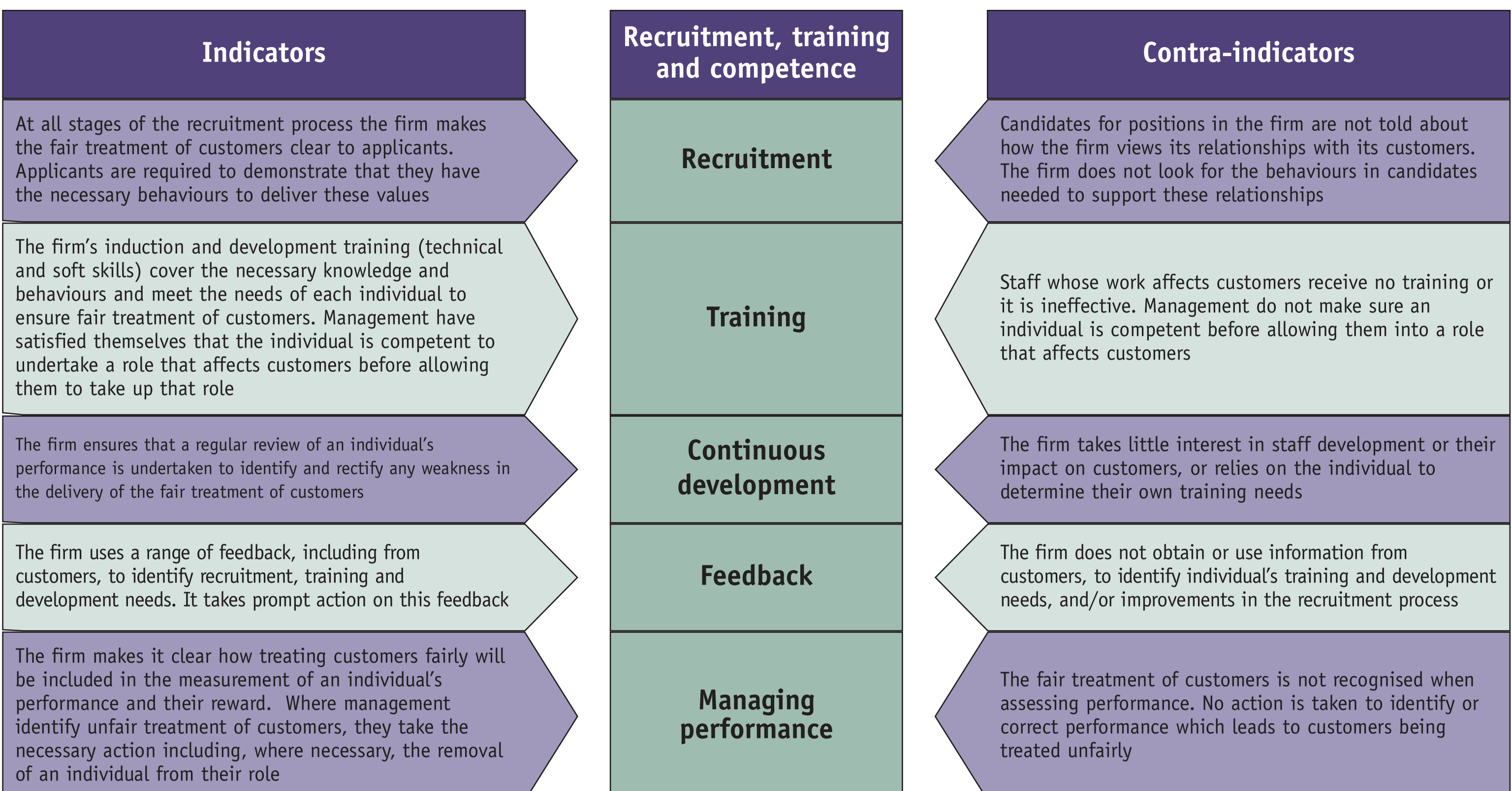
Indicators	Business decisions	Contra-indicators
The firm plans its business by taking the fair treatment of customers into account	**Business perspective**	The firm plans its business in a way that does not give regard to the fair treatment of customers
The firm uses customer surveys and other feedback (e.g. complaints) to improve processes and procedures	**Customer perspective**	The firm does not seek external feedback or use the feedback that comes to it
The firm undertakes its day-to-day business by taking the fair treatment of customers into account. Individuals have the necessary skills and expertise to make fair decisions, or where they do not, they understand the need to refer. The records of decisions about customer issues are maintained for the appropriate length of time	**Customer decisions**	The firm undertakes its day-to-day business in a way that does not recognise the fair treatment of customers. Individuals lack the necessary skills to make fair decisions and generally favour the firm's interests over those of the customer. Records of decisions about customers issues are not kept
The firm allocates enough resource to enable it to treat its customers fairly in a timely manner	**Resources**	There is little or no recognition of the resource required to ensure that customers are treated fairly when business plans are made, or the required resource is late
Management develop staff and systems in line with the actual or planned growth of the business in order that customers are treated fairly	**Learning and growth**	The business is being developed without a complementary plan to grow staff and systems to ensure the fair treatment of customers

Annex 2

Controls – indicators and contra-indicators for smaller firms



Recruitment, training and competence – indicators and contra-indicators for smaller firms



Indicators	Recruitment, training and competence	Contra-indicators
At all stages of the recruitment process the firm makes the fair treatment of customers clear to applicants. Applicants are required to demonstrate that they have the necessary behaviours to deliver these values	**Recruitment**	Candidates for positions in the firm are not told about how the firm views its relationships with its customers. The firm does not look for the behaviours in candidates needed to support these relationships
The firm's induction and development training (technical and soft skills) cover the necessary knowledge and behaviours and meet the needs of each individual to ensure fair treatment of customers. Management have satisfied themselves that the individual is competent to undertake a role that affects customers before allowing them to take up that role	**Training**	Staff whose work affects customers receive no training or it is ineffective. Management do not make sure an individual is competent before allowing them into a role that affects customers
The firm ensures that a regular review of an individual's performance is undertaken to identify and rectify any weakness in the delivery of the fair treatment of customers	**Continuous development**	The firm takes little interest in staff development or their impact on customers, or relies on the individual to determine their own training needs
The firm uses a range of feedback, including from customers, to identify recruitment, training and development needs. It takes prompt action on this feedback	**Feedback**	The firm does not obtain or use information from customers, to identify individual's training and development needs, and/or improvements in the recruitment process
The firm makes it clear how treating customers fairly will be included in the measurement of an individual's performance and their reward. Where management identify unfair treatment of customers, they take the necessary action including, where necessary, the removal of an individual from their role	**Managing performance**	The fair treatment of customers is not recognised when assessing performance. No action is taken to identify or correct performance which leads to customers being treated unfairly

Reward – indicators and contra-indicators for smaller firms

Indicators	Reward	Contra-indicators
The firm has performance related salary for staff which recognises the quality of their interaction with customers and the outcomes they deliver. Management make the structure transparent to all employees	**Salary**	Salary is heavily affected by sales or volumes without consideration of quality. Performance development plans incentivise staff to give inadequate service to customers or create the risk of unfair treatment of customers (e.g. encourages staff to pursue quantity at the expense of quality)
When setting commission levels, management recognise qualitative issues such as persistency and complaints. Some recommendations made by advisers do not generate commission	**Commission**	Advisers only have sales and product targets, with few or no quality indicators. Commission is paid up-front without any clawback for inappropriate sales
The firm makes the bonus and profit share framework transparent for all staff and the level of reward takes account of the fair treatment of customers	**Bonus and profit share arrangements**	The level of reward is calculated solely on the extent of income generated and/or growth, disregards the fair treatment of customers and/or is not transparent
The firm treats all staff fairly and understands the impact both formal and informal recognition has on staff. The firm's success measures recognise the importance of the fair treatment of customers	**Recognition**	Management give informal or formal recognition to employees that excel in making profit or sales without consideration of the fair treatment of customers. These actions encourage other employees to act in the same way

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