

Market Conduct Supervisory Approach

The global financial crisis highlighted the potential for market conduct issues to result in large-scale losses to consumers and cause widespread disruption to financial institutions and markets, as was evident in the mis-selling of mortgage products in the United States. Since then, there has been renewed regulatory focus on the importance of establishing effective oversight arrangements to ensure that financial institutions conduct business in a responsible manner, while empowering consumers to make informed financial decisions. This requires an appropriate regulatory framework and a credible supervisory process that is proportionate to the risks that consumers may face from improper business practices of financial service providers (FSPs).

The Bank regulates 298 FSPs offering a broad spectrum of products and services to retail consumers in the banking, insurance and takaful sectors. Given such a wide remit and the increasing importance of managing market conduct risk in a more competitive and complex environment, the Bank has strengthened its market conduct supervisory approach in 2011 with the aim of: (i) improving the prioritisation of market conduct issues and institutions for supervisory attention; and (ii) improving the Bank's engagements with FSPs, particularly with the institutions' senior management and board, on market conduct developments and concerns. These enhancements involve the principles that: (i) the board and senior management of FSPs must be primarily responsible for ensuring fair conduct towards consumers; and that (ii) consumers have an important role in protecting their own interests by using available avenues to seek information and redress, and to engage more actively with FSPs in making their financial decisions. The enhancements will enable the Bank to allocate its supervisory resources more optimally to key market conduct risks which have the highest potential for causing widespread detriment to consumers or a general loss of confidence in the financial system, and will also support the Bank's more forward-looking and preventive interventions.

A central piece of the enhanced supervisory approach involves changes in the manner in which the Bank obtains and analyses consumer information. Sources of information have been significantly expanded from mainly complaints and submissions of product information, to include a more regular cycle of direct feedback obtained from engagements with consumers, as well as observations from the Bank's assessments of the significant activities and control functions of institutions supervised by the Bank. Conversely, any material concerns identified through the Bank's market conduct reviews will form inputs to the Bank's prudential assessments to the extent that it increases an institution's potential exposures to financial losses due to legal or regulatory actions, loss of reputational goodwill, or collective behaviours of FSPs that contribute to heightened systemic risks as experienced during the subprime crisis. The Bank will also leverage on its presence throughout the country to obtain early indications of unhealthy practices in specific localities before they spread to other parts of the country. In addition, the Bank intends to review the scope and form of current complaints and product information reported to improve the quality and consistency of the data collected for purposes of its risk analysis.

The Bank will use this information to detect new trends in product innovations and distributions that carry inherent risks to consumers, and to support more complete cross-sectoral and industry-wide assessments of risks which form the basis of the Bank's thematic reviews. This will provide a deeper understanding of the factors that influence consumer behaviours. For this purpose, the Bank will begin work in 2012 to examine how consumers relate their decision-making to general or specific information provided on financial products and services, and the factors that promote or impede the ability of consumers to change FSPs. The Bank will also begin gathering more detailed information to understand the ways in which the interplay between collective actions of FSPs and consumer behavioural biases can increase systemic risks.

The Bank's strengthened analysis of market conduct risk will drive several other important changes in its supervisory approach. Thematic work, targeting specific products, services and practices identified through the Bank's risk analysis, will assume a more prominent role in the Bank's approach. This allows

for dealing more comprehensively across the industry with identified conduct risks, strong signalling effects of areas of concern to the Bank, and greater impact achieved from more targeted and coordinated interventions applied consistently across FSPs.

The Bank will complement its thematic work with the current review of market conduct practices of individual financial institutions. However, this will be based on an enhanced process for identifying institutions that will be subject to individual monitoring and that will attract greater supervisory attention. The Bank expects to complete a baseline assessment of the most active banking institutions, insurers and takaful operators in the retail market, based on considerations of size, profile of target market, product complexity and distribution channels, by mid-2013. This work has already started and is based on a more structured framework to assess how well an FSP is controlling its conduct risks. FSPs will be assessed against expectations of fair and responsible practices which are enumerated in various guidelines and circulars issued by the Bank across seven key areas: (i) product development and governance; (ii) transparency and disclosure of information; (iii) sales and marketing practices; (iv) after-sales support; (v) personal data protection; (vi) management and control of third party service providers; and (vii) advisory and redress channels. The baseline assessment will drive the intensity of the Bank's supervisory activities for such individual institutions. The Bank will maintain an ongoing review of all institutions identified for individual monitoring to track developments that may alter the baseline assessment and by extension, the level of supervisory intensity applied to them.

As highlighted earlier, a higher level of engagements with FSPs represents an important aspect of the Bank's enhanced supervisory approach. The implementation of a more consistent framework for supervisory assessments in the area of market conduct will enable the Bank to engage FSPs more constructively on its market conduct concerns. The assessments also aim to bring greater focus by the board and senior management on their critical role in promoting an institution-wide culture of ethical and responsible dealings in their conduct of business. This includes their role in setting remuneration policies, and ensuring that conduct issues are given appropriate attention in the institution's operational and risk management activities. The board and senior management will be accorded greater accountability for conduct failures. The Bank's interactions with FSPs will continue to be closely coordinated across the supervisory functions of the Bank to reduce duplicative burdens on FSPs. This will also promote greater focus on the growing interaction between the management of financial and market conduct risks.