



FAIS CONFERENCE March 2016 Part 2



Content



Registration and Licencing – issues of common concern

Supervision feedback on developments

Feedback on FIC Inspections



Registration And Licencing – Issues Of Common Concern

OVERVIEW

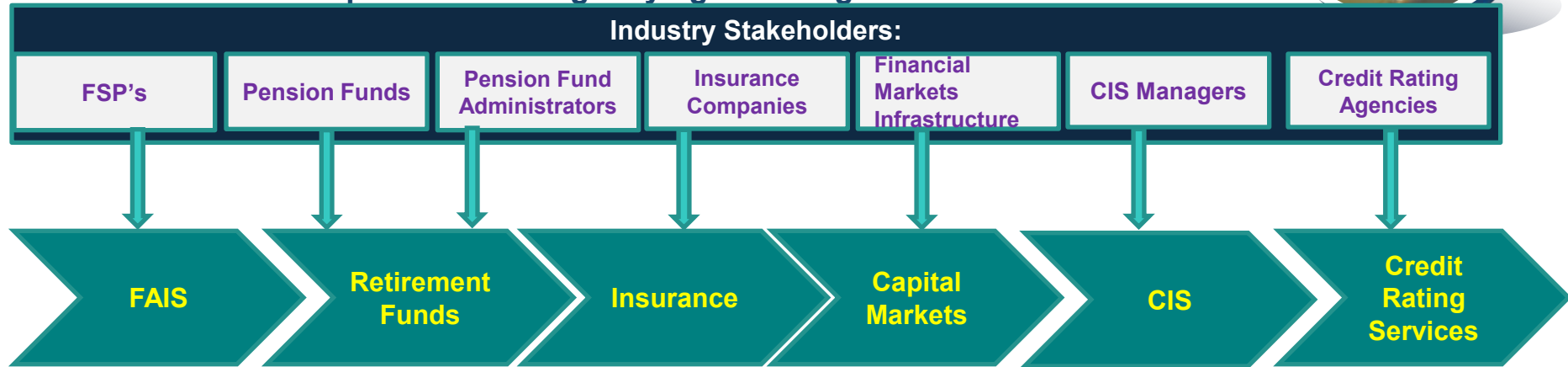


- ❖ **FSB'S Current Licensing / Registration Approach**
- ❖ **Business challenges – System Challenges**
- ❖ **Drivers for Change**
- ❖ **Interim Solution Overview**
- ❖ **Process improvement in FAIS in-line with the changes**
- ❖ **Importance of Data**

FSB'S Current Licensing / Registration Approach



In the current licensing approach, each type of institution is registered or approved by the different FSB line departments using varying licensing criteria and standards.



Different Legislations

<ul style="list-style-type: none"> Financial Advisory and Intermediaries Services Act (FAIS Act)(Act 37 of 2002) 	<ul style="list-style-type: none"> Pension Funds Act, 24 (Act 24 of 1956) Friendly Societies Act (Act 25 of 1956) 	<ul style="list-style-type: none"> Long-term Insurance Act (Act 52 of 1998) Short-term Insurance Act (Act 53 of 1998) 	<ul style="list-style-type: none"> Financial Markets Act (Act 19 of 2012) 	<ul style="list-style-type: none"> Collective Investment Schemes Control Act (Act 45 of 2002) 	<ul style="list-style-type: none"> Credit Rating Services Act (Act 24 of 2012)
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Organisational Structure

<ul style="list-style-type: none"> Sole proprietor Company Pty (Ltd) Close Corporation Trust Partnership Unions Limited Companies 	<ul style="list-style-type: none"> Unions Limited Companies Bargaining Councils Self-Standing Funds Umbrella Funds 	<p>Limited Companies</p>	<ul style="list-style-type: none"> Company Pty (Ltd) Limited Companies 	<ul style="list-style-type: none"> Company Pty (Ltd) Limited Companies 	<ul style="list-style-type: none"> Company Pty (Ltd) Limited Companies
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Business challenges – System Challenges



The current regulatory systems lack the integration capability to allow for the single view of the customer across the various line divisions

**No single view of
customer profile**

System Challenges

- No single view of customer profile
- Finance – multiple systems (different magic platform) to process various departmental fees / levies / contact details
- Duplication of data
- Poor data quality
- Multiple platforms to support and maintain
- Fragmented access
- Systems not real-time
- System not agile (not receptive to change)
- Inflexible architecture

FSB's Drivers For Change



Drivers for Change

Policy

- Legislative requirements (New Twin-Peaks)
- Sounder and better regulated financial services industry
- Broaden economic participation and contribution
- Promoting a compliance culture and morality
- Protecting economy and society

Financial Institution Expectations

- Convenience and ease of doing business
- Improved technology capabilities to ensure effective and efficient stakeholder interaction
- Enhance compliance processes
- Reduced cost of compliance
- Efficient and effective professional service

Consumer Expectations

- Protection of consumers of financial services and products
- Transparent and consistent service delivery
- Efficient and effective professional service

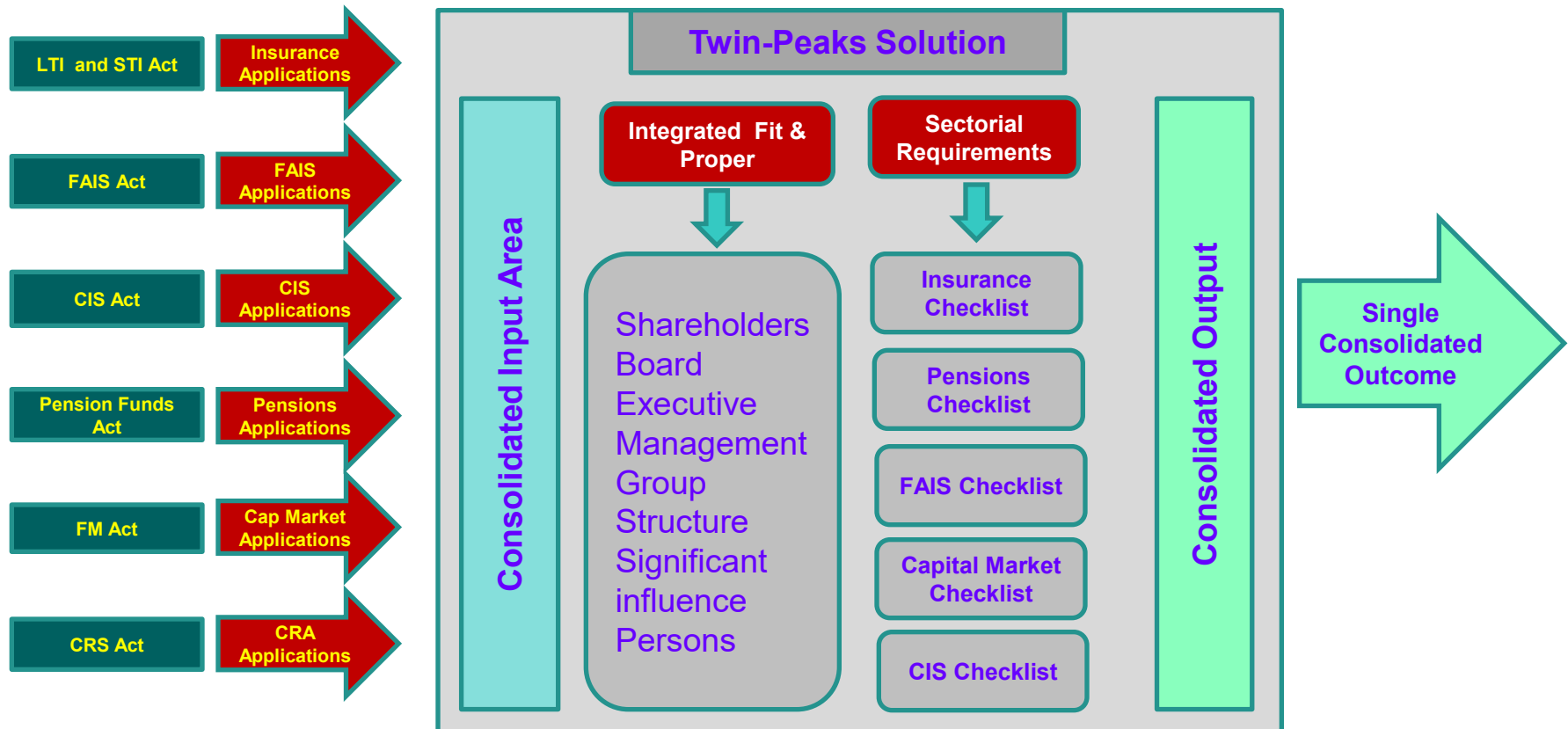
Internal

- Adherence to best international practices
- Enhancing human capacity
- Efficient delivery – more with the same
- Build a sustainable and flexible organisation
- Understanding our stakeholders business and roles
- Ability to manage risk
- Flexible Systems to adopt to changing environment

Interim Solution Overview



- The interim solution will be applicable during the transitional period of the FSCA
- The solution will have centralised fit & proper capabilities
- This means that the existing sectorial legislation will still be relied upon to conduct regulatory activities
- Information required during licensing applications based on sectorial acts



Process improvement in FAIS in line with the changes



1. On-line licence applications
2. FSP form 4 automatic pre-population
3. Automated Allocation of tasks – compliance reports
4. On-line profile changes
5. Single client view for regulatory purposes
6. Exemption Workflow introduced, more stringent monitoring of exemptions
7. A system was developed and implemented for the electronic submission of Assets Under Management for levy purposes.
8. Data Dumping or Web based Access for MIE, Lexis Nexis, Astute
9. Improved process for DOFA verification

Importance of Data



Section 1 of the licence condition/restriction:

“The financial services provider must inform the Registrar in writing, by facsimile or in an appropriate electronic format, within 15 days after change has taken place, of any change in respect of business information”.

Top 5 Information that FSPs’ forget to update:

- ❖ **Contact details;**
- ❖ **That representatives who were appointed under supervision are no longer working under supervision;**
- ❖ **Details relating to the management of the FSP (directors, members, shareholders etc.);**
- ❖ **That they have ceased / started receiving client funds and / or premiums;**
- ❖ **Change in their financial year end**



SUPERVISION FEEDBACK ON DEVELOPMENTS



Contents



9699 (Category I)

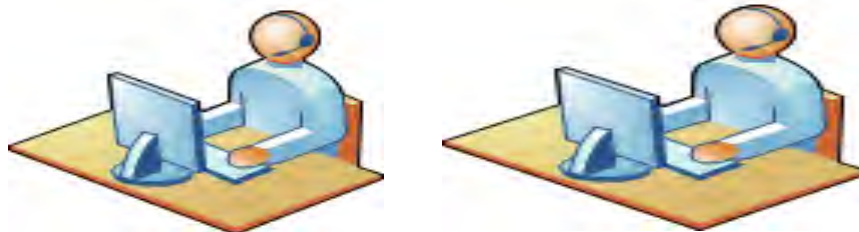
693 (Category II and IIA)

27 (Category III)

94 (Category IV)

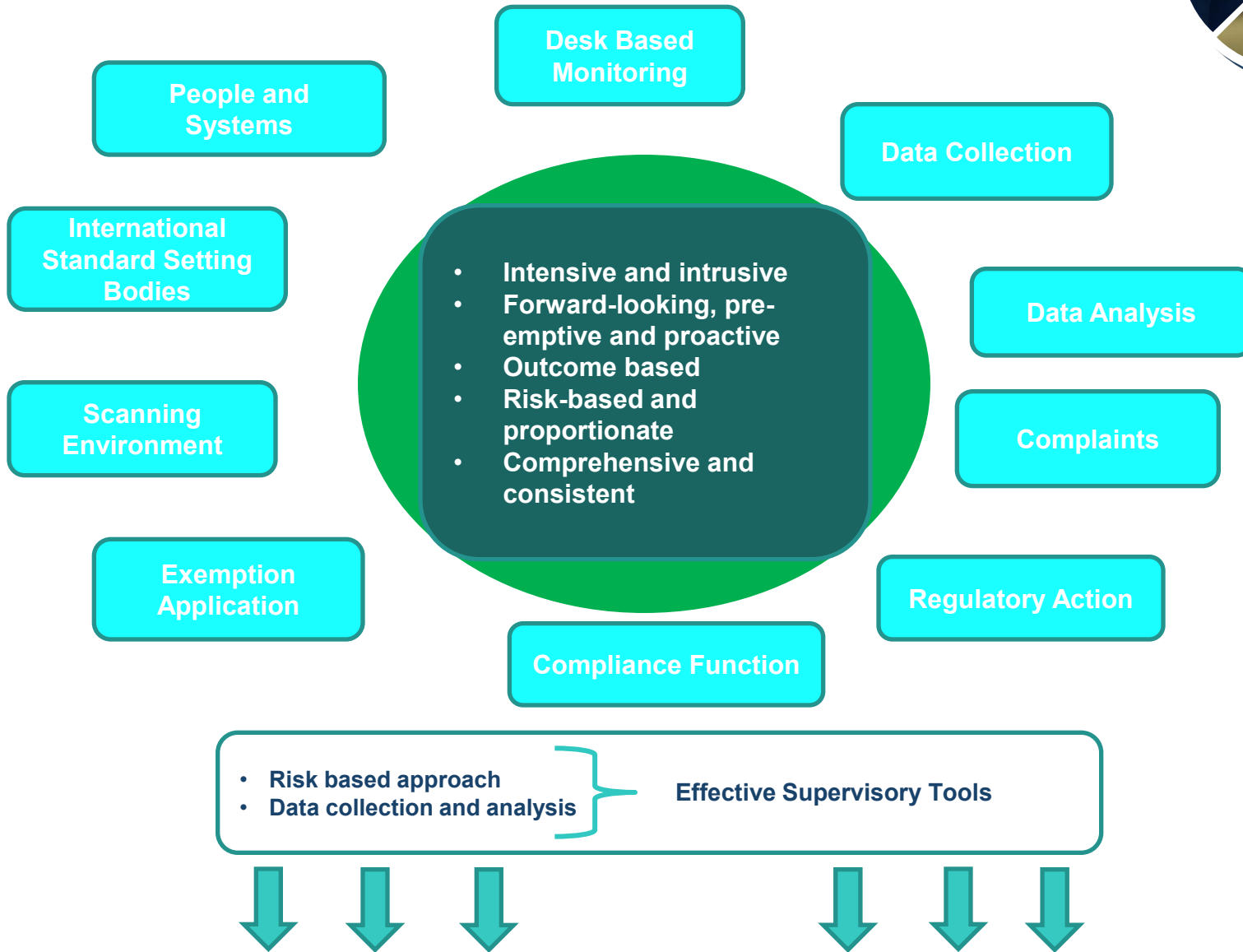
4 035 Approved Compliance Officers

**10 513
FSPs**



**132 FAIS Division Staff Complement
65 (FAIS Supervision Department)**

Data Management & Collection



Theme Visits



2014 / 2015 / 2016

Category I (without compliance officers)

- Contravention of General Code of Conduct
 - ❖ Professional indemnity cover
 - ❖ Keeping and maintenance of records, including records of advise
 - ❖ Risk management
- Contravention of financial soundness requirements

Category I (Direct Marketers)

- Advice vs. factual information
- Definition of intermediary services
- Appointment of FAIS representatives
- Non compliance with the competency requirements
- Quality assurance

Category IV

- Non-compliance with licensing conditions
- Relationship between FSP and juristic representatives
- Compliance monitoring
- Non-compliance with FICA provisions
- Financial solvency requirements

Theme Visits



2014 / 2015 / 2016

Category II and IIA

- Financial soundness requirements for juristic representatives
- Adoption of risk sensitive formula
- Compulsory review of internal controls by an objective and independent party
- Early warning requirements

Category III

- Unregistered CIS funds on LISP platforms
- Ownership of clients
- Re-mandating of clients

Conduct Of Business Report



Adopting the new approach to supervision aims to:

- Ensure that we are intensive, intrusive and proactive in our supervision of FSPs;
- Ensure a shift from a rules and compliance based supervisory approach to an outcomes based approach;
- Ensure that the report is customised to the nature and type of business conducted by different categories of FSPs; and
- Data collection, analysis and identification of trends.

Phase 1 consultation:

Market Conduct Regulatory Framework Steering Committee

Phase 2 consultation:

Industry consultation



Sign-on bonuses

Board Notice 146 (04 December 2014)

The Registrar prohibited category 1 FSPs that is authorised to give advice from receiving a sign-on bonus from any person, and also prohibits any person from offering or providing a sign-on bonus as an incentive to become a category I provider to give advice. The only exception is a new entrant, who is allowed to receive a sign-on bonus. This went into effect on 4 December 2014. Notice to this effect was given on 1 September 2014.

Board Notice 122 (March 2015)

The Registrar requested registered long-term insurance companies who are also authorised FSPs to submit a special compliance report. The purpose of this report was to determine the payment of sign-on bonuses, and the extent to which this could be linked to churning of policies by the recipients of the sign-on bonuses. Respondents were asked to provide feedback in terms of 3 periods:

Special Compliance Reports



Sign-on bonuses

01 September 2012 – 31 August 2014

Number of FSPs	No of FSPs (Sign on bonuses paid)	Recipients of bonuses	New policies	Replacement policies
46	6	1366	101 278	43 816 (43%)

01 September 2014 – 31 March 2015

Number of FSPs	No of FSPs (Sign on bonuses paid)	Recipients of bonuses	Replacement policies (Risk)	Replacement policies (Investments)
46	4	548	604	137

After effective date 04 December 2014

- Contracts signed up to 03 December 2014
- Payments were made after the effective date up to 2015

Way Forward



Theme visits

Type of FSP	Focus Area
Small FSPs without compliance officers	<ul style="list-style-type: none">• Compliance with the General Code of Conduct• Fit & proper requirements
Category I FSPs - high, medium-high and medium impact FSPs	<ul style="list-style-type: none">• Compliance with section 13(1)(c) of the FAIS Act• Effectiveness of the compliance officers in the business
Hedge Fund FSPs	<ul style="list-style-type: none">• Where onsite reviews were last conducted before 2014• High risk investment activities and all hedge fund managers are visited every two years.
Category II FSPs	<ul style="list-style-type: none">• Financial soundness requirements for juristic representatives• Adoption of risk sensitive formula• Compulsory review of internal controls by an objective and independent party• Early warning requirements
Category III FSPs	<ul style="list-style-type: none">• Ownership of clients• Re-mandating of clients• Unregistered funds on LISP platforms• Nominees

New Developments



- **Conduct of Business Report**
- **Change of financial soundness requirements for Cat II, IIA and III**
- **Review framework for Cat III**
- **Impact study on Small FSP intervention**
- **Review Cat IV requirements**
- **Framework for crowd funding**



FEEDBACK ON FIC INSPECTIONS

FICA inspections



- Undertaken inspections pursuant to Section 45B
- Optimise resources and skills
- Conducted alongside risk assessments and theme visits
- Purpose of inspections – to determine the level of compliance of the AIs with FICA

Scope



Duty to identify and verify clients – Section 21

Duty to keep records - Section 22

Duty to report to the FIC:

- ❖ Cash Threshold Reports - Section 28
- ❖ Terrorist Property Reports - Section 28A
- ❖ Suspicious Transaction Reports - Section 29

Administrative Duties:

- ❖ Duty to formulate Internal Rules - Section 42
- ❖ Duty to provide training - Section 43(a)
- ❖ Duty to appoint a Compliance Officer - Section 43(b)

Duty to Register with FIC – Section 43B

International best practice

Scope



- ❖ FICA mitigates the risk of money laundering
- ❖ Control procedures provoke fear of penalties and reputational damage.
- ❖ Allegations of money laundering may be an indication that AI does not comply with FICA and may trigger an inspection
- ❖ Embark on regulation and supervision that goes no further than is necessary but still achieves the stated objectives
- ❖ Cannot use inspection powers to investigate money laundering
- ❖ Referral of money laundering and criminal activities

Inspection process



- ❖ A key focus of inspection process is assessing:
 - ❖ governance, systems, controls
 - ❖ Compliance with FICA requirements
 - ❖ Rules and assess evidence of compliance.
- ❖ Forward looking in assessing the:
 - ❖ business models,
 - ❖ strategies
 - ❖ risk management frameworks
 - ❖ to form our own judgement on the associated risks.

Inspection process



Planning & Preparation

- Information gathering
- Data analysis

Define Inspection activities

- Scope
- Resources

Conduct Inspection

- Interviews
- Reviews
- Testing

Reporting

- Findings
- Recommendations

Follow up

- Implement
- Monitor

Findings



Based on sample of AIs of varying sizes
Issues are representative of our observations across the sample

1. Identity verification & record keeping:

- ❖ Qualifying entities
- ❖ Verification documents
- ❖ Inadequate information on legal entities
- ❖ It is possible that documents were obtained
- ❖ Lax internal controls
- ❖ No awareness of the basic requirements
- ❖ Non adherence to AML/CFT policies
- ❖ Risks of not implementing a KYC or CIV policy
- ❖ National FICA solution

Findings



2. Cash threshold reporting

- ❖ Als do not receive cash
- ❖ Requirement to report cash transactions
- ❖ Cash deposited in the bank account of the AI/RI is not reported
- ❖ No procedure to detect and submit reports to FIC

3. Terror property reporting

- ❖ Requirement to report terrorist related property
- ❖ No procedure to detect and submit reports to the FIC
- ❖ No screening of clients – inadequate or inconsistent
- ❖ Sanction lists - Worldcheck for PEPs list and UN 1267 list

Findings



4. Suspicious & unusual transaction reporting

- ❖ Applies to any person
- ❖ AIs were aware of the requirement to submit STRs to the FIC
- ❖ No knowledge of suspicious activities in the AI's environment
- ❖ Outsourcing the reporting obligation to external compliance officer or administrator with signing powers on the bank account
- ❖ Some transactions may not be reported where the AI employs centralised function for boarding clients

Findings



5. Internal rules

- ❖ Every AI is to formulate and implement internal rules
- ❖ Internal rules or AML/CFT policies and procedures
- ❖ Generic, outdated and unsigned. Also inaccurate and irrelevant.
- ❖ Ensure AML/CFT policies and procedures are up to date
- ❖ Customised and aligned to the business of the AI
- ❖ Simplified and easy to understand
- ❖ Approved by senior management of the AI
- ❖ Roles and responsibilities of the various people involved in ensuring AML/CFT compliance
- ❖ Working methods and processes to deal with these functions
- ❖ Disciplinary action against staff for non-compliance

Findings



6. Training

- ❖ Provide training to staff
- ❖ Level of training
- ❖ Training focused on FICA only
- ❖ The training provided to the employees of AI seemed inadequate or not frequent enough
- ❖ Remembering the training and knowledge of FICA
- ❖ Refresher training

7. Appointment of the compliance officer

- ❖ Roles of the MLRO and compliance officer

Findings



8. Registration:

- Every AI (Schedule 1) and every RI (Schedule 3) must register with FIC
- Having other products on the licence
- Conduct business of more than one AI
- A large number of AIs/RIs are still unregistered

Findings



9. High risk clients

- ❖ AIs are prone to do business with high risk clients
- ❖ PEPs
- ❖ Clients are not risk rated for AML/CFT purposes
- ❖ Conduct own risk assessments, characterise clients and apply proportionate measures
- ❖ Separate procedures for dealing with high risk clients

Follow up



- Purpose of the inspections
- Action taken was proportionate
- Identified risk was mitigated
- Action recommended - nature, scale and potential impact of the risk or shortcomings.
- Follow up to ensure that undertakings and commitments are delivered on
- Where AI cannot, or do not, take appropriate action – use supervisory powers to force a resolution.
- Consider imposing sanctions

FICA amendments



- ❖ Higher effectiveness can be attained if AIs share the burden of risk assessments
- ❖ Sometimes reaching prescribed level of requirements is not enough
- ❖ Proposed amendments
 - ❑ Risk Based Approach
 - ❑ On-going due diligence
 - ❑ Source of funds and wealth
 - ❑ Ultimate beneficial ownership
 - ❑ Domestic Prominent Influential Persons & Foreign Prominent Public Officials