VERBATIM

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THE CONDUCT OF FINANCIAL INSTITUTIONS BILL (COFI)

KEEP AN EYE ON IT AND START NOW

If there is one piece of legislation to keep an eye on going forward, as far as employee benefits is concerned, it is this one. All financial institutions, including retirement funds and administrators need to be very sure they understand this piece of draft legislation and what is coming down the line as it fundamentally shifts legislative requirements and requires a good understanding in order to implement.

Although the effective date of COFI is some time off (about three years away), given what COFI requires, financial institutions are going to need to apply their minds to it and start moving toward compliance with COFI long before the effective date. In addition, the FSCA is going to need to gear up significantly in order to effectively regulate and supervise under COFI. If the FSCA does not set up the necessary structures, resourcing, analytics and other requirements, COFI will be a damp squib. If the FSCA gets it right, on the other hand, COFI will have a deep impact on our industry.

COFI AND THE FSRA WORK TOGETHER

The Conduct of Financial Institutions Bill (“COFI”) was issued hot on the heels of the implementation of the Financial Sector Regulation Act (FSRA”). The two pieces of legislation complement each other and work together.

The FSRA establishes the regulator entities, such as the Financial Sector Conduct Authority (“FSCA”) and the Prudential Authority and provides them with additional and extensive powers and, thus, is said to be regulator-facing. COFI, on the other hand, is intended to be the central piece of legislation regulating the conduct of financial institutions and other entities and, thus, is said to be regulated entity-facing.

While the FSRA applies to many regulators, including the FSCA and the Prudential Authority, COFI is only applicable to the entities that the FSCA regulates. This is because COFI regulates market conduct, which is the purvey of the FSCA. Refer to diagram on the following page.

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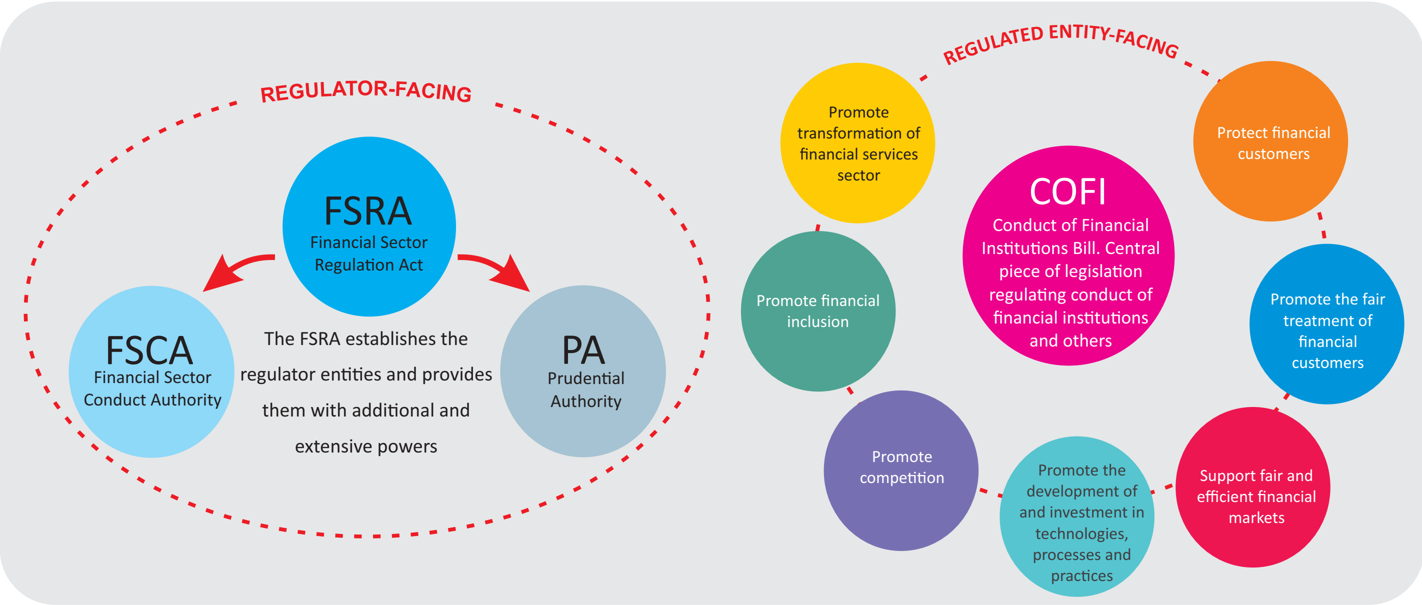

COFI WILL STREAMLINE THE LEGISLATION

It is intended that COFI streamline most of the legislation related to conduct standards currently applicable to financial institutions. COFI is intended to entirely replace the many pieces of legislation currently in existence (for example the Financial Advisors and Intermediary Services Act and the Collective Investment Schemes Control Act) or, alternatively, the majority of the provisions of the Act (for example the Pension Funds Act). The Treating Customers Fairly Principles are entrenched into legislation through COFI.

CONDUCT STANDARDS

The FSRA allows regulators to issue conduct standards on an enormous array of matters affecting financial institutions. Many of these conduct standards are currently being drafted by the FSCA and will then simply continue in place under COFI. This means that the implementation of many of the principles and outcomes included in COFI will be done before COFI becomes effective. Effective complaints management by financial institutions is a good example of this.

WHO FALLS UNDER COFI?

All financial institutions providing a financial product or financial service and that must be licensed fall under COFI, this includes section 13B administrators, retirement funds, banks, insurers, collective investment schemes and asset managers. Even entities that are not required to be licensed under COFI (especially those that have dealings with retirement funds) will fall under this Act and be supervised by the FSCA, such as sponsors of umbrella funds. In addition, COFI includes requirements for natural persons performing crucial roles like the CEO, members of a fund's board of management, risk managers, governing bodies, directors, compliance officers and actuaries. Both retail and non-retail markets are included within the provisions of COFI.

PRINCIPLE-BASED LEGISLATION

COFI is principle- based legislation. This means that we are required to comply with the principles set out in COFI and not a list of requirements (although there will be those too). COFI sets out a number of principles and the outcomes that entrench those principles. Thus, the tick-a-box approach to compliance will become a relic.

Where financial institutions do not move with the times and replace outdated compliance and risk programmes with compliance to principles (and monitoring, reporting and taking action based on outcomes) they will find themselves possibly subject to *enforcement action based on non-compliance with principles*. This is extremely important and requires a shift in the way that the employee benefits industry does business. Financial institutions may find that they have ticked all the boxes (for example, policies, procedures, communication, risk programmes, etc.) but they have still not met a principle. Being able to practically demonstrate achievement with outcomes will become the focus.

WHAT DOES COFI COVER?

COFI covers a wide-range of topics, including those set out below:

- Fit and proper requirements, operational and governance requirements, a number of mandatory policies
- Principles and requirements around financial products and services, specific identification of customer needs, including product design, product/service development requirements (that incorporate specific sign-offs by senior management)
- New licensing structure and requirements
- Transformation principles (including the submission of a policy to the FSCA and enforcement action to ensure compliance)
- The protection of personal information
- Promotion, marketing and disclosure principles
- Principles when changing and switching investment's and submitting claims
- Complaints management
- Distribution, advice and discretionary investment management
- The safe custody, control and administration of the assets of a financial institution
- Reporting to the FSCA
- Offences

COFI AND RETIREMENT FUNDS

As it is a financial institution, a retirement fund currently regulated under the Pension Funds Act will fall to be regulated under COFI as well. The Board is responsible for compliance with COFI and must inform the FSCA if the fund has materially not complied with its provisions.

Public sector and state retirement funds may also be regulated under COFI (this is under discussion and the draft wording of COFI already permits it).

Retirement funds, under COFI (once effective), will be registered by both the FSCA and the Prudential Authority. There will be a phasing-in period for this.

Conduct standards currently applicable and being drafted by the FSCA, will be migrated from the Pension Funds Act to COFI.

Professional fiduciaries, such as independent and professional board members will be required to be licensed by the FSCA and will be subject to fit and proper requirements. Employer, employee and sponsor-appointed board members will not be required to be licensed but will have fit and proper requirements and be required to continually develop their skills.