



## INDEPENDENT PRINCIPAL OFFICERS – FSCA COMMUNICATION 7 OF 2019

### THE FSCA COMMUNICATION - BACKGROUND

The Financial Services Conduct Authority (FSCA) issued Communication 7 of 2019 (the Communication) on 12 December 2019. The Communication provides information about Directive 8 of 2018 (the Directive).

While a Communication is not law, it should be noted that the Communication is about a Directive, and a Directive has the same binding effect as legislation.

### WHAT WAS DIRECTIVE 8 OF 2018 ABOUT?

Directive 8 (Prohibition on the Acceptance of Gratification) was issued on 8 March 2018 to assist in combatting and preventing corruption and corrupt activities in the retirement fund industry.

Directive 8 imposes conditions to combat and prevent bribery and corrupt conduct by principal officers, deputy principal officers, board members, employees of retirement funds, valuers, auditors, administrators, employees of administrators, other officers or other service providers to funds including investment managers and investment advisors.

The general principle is that the above-mentioned fund officials, fund stakeholders and fund service providers must not be involved in any conduct which constitutes bribery, fraud or corruption. This conduct will have a bearing on fitness and propriety to hold office or provide a service.

Specific types of gratification are automatically not permitted to be offered or received, this includes any **gratification** which objectively viewed, creates a conflict of interest with the receiver's fiduciary duty towards the fund.

The definition of "gratification" includes, among other things: any office, status, honour, **employment**, contract of employment or services, any agreement to give employment or render services in any capacity.

In addition, the above-mentioned fund officials, fund stakeholders and fund service providers must **report** or disclose to the FSCA any breach or attempted breach of the Directive immediately upon becoming aware of this breach. The FSCA's Information Circular 1 of 2018 gives guidance on how to report or disclose matters to the FSCA.

### WHAT IS THE MAIN ISSUE BEHIND THE COMMUNICATION?

The Communication looks to clarify, mainly, that a principal officer of a fund, as a result mostly of the extracts set out above from the Directive, may not be both the principal officer of a fund and employed by the same fund's service provider at the same time. This has been a fairly wide-spread practice in the industry, especially amongst umbrella funds, where the principal officer of the fund is also often employed by the administrator or consultant of the fund, who is generally the sponsor of the fund.

After pointing out the provisions of the Directive as well as the duties and responsibilities of principal officers, the FSCA concludes that:

“... the simultaneous employment of the principal officer by a service provider is impermissible and is also undesirable. The principal officer's ability to comply with his/her duty to report on the activities of such service provider is likely to be impaired by virtue of their employment relationship with the service provider ... To ensure a principal officer's independence, it is desirable that the principal officer is employed directly by the fund and is not in receipt of any type of prohibited gratification”.

### WHAT DOES THE FSCA WANT A FUND TO DO IF ITS PRINCIPAL OFFICER IS EMPLOYED BY A SERVICE PROVIDER TO THE FUND?

#### (a) Enter into an Enforceable Undertaking

Firstly, the FSCA will be writing, or has written, to the funds where the principal officer is employed by a service provider to obtain an Enforceable Undertaking. This Enforceable Undertaking will include the fund, the service provider, the Principal Officer and any other party that is included in the arrangement.

The Enforceable Undertaking will include wording to the effect of what **future actions** the parties will take to **put the situation right** (remedies) and in what period of **time** these actions will take place, so as to reach compliance with the Directive.

The Communication specifies that the Enforceable Undertaking will allow funds and the relevant parties a maximum **period of 6 (six) months** within which to regularise the appointment of a new principal officer.

#### *What is an Enforceable Undertaking?*

Under the Financial Sector Regulation Act, a person may give a written undertaking:

- to a Responsible Authority, in this case the FSCA
- about their future conduct.

If the undertaking is accepted by the FSCA this becomes an Enforceable Undertaking.

#### *Enforceable Undertakings should not be taken lightly as:*

- every Enforceable Undertaking (with very limited exceptions) is published;
- the FSCA can suspend or withdraw licenses if the Enforceable Undertaking is breached or the Financial Services Tribunal can be asked to order a person to comply, order specific actions and make other orders. The FSCA can then file a copy of the Tribunal's order with a court – which gives the order the effect of a civil judgment;
- the FSCA can also impose an administrative penalty for breach of an Enforceable Undertaking; and
- in addition, if an Enforceable Undertaking is breached, the FSCA may (in certain circumstances) issue a Directive to comply with an Enforceable Undertaking and it is an offence not to comply with a Directive.

It is possible that an Enforceable Undertaking could also lead to loss of business as it is likely that funds looking for a provider may ask the provider if they have ever entered into an Enforceable Undertaking or they could just look for them on the FSCA's website.

#### (b) Contact the FSCA

The FSCA wants funds and principal officers where the principal officer is in a service provider's employ to contact them if they have not yet been contacted by the FSCA.

The person to contact at the FSCA is Naheem Essop at email address: [naheem.essop@fsc.co.za](mailto:naheem.essop@fsc.co.za).

#### WHAT HAPPENS IF I DON'T COMPLY WITH THE COMMUNICATION?

Enforceable Undertakings are used mostly, at the moment, as a lighter form of enforcement action. If funds, service providers and principal officers do not co-operate readily or do not agree with the Enforceable Undertakings, the FSCA may take other forms of enforcement actions (as permitted in the Financial Sector Regulation Act) which are many and varied, for example administrative penalties.