

THE FINANCIAL SECTOR REGULATION ACT, 2017 – THE TWIN PEAKS REGULATORY FRAMEWORK

The President has signed the Financial Sector Regulation Act into law ('the Act'), introducing the twin peaks regulatory framework to South Africa.

The effective date(s) of the Act are not yet known. Different effective dates will apply to different sections of the Act.

Whilst the Act comes into force over a period of time, there is bound to be overlap between the Act and the Pension Funds Act.

The purpose of the Act

The Act will establish a regulatory and supervisory framework that promotes financial stability, fair treatment, and protection of customers as well as financial inclusion.

It also focuses on the efficiency and the integrity of the financial system, building confidence in the financial sector through transformation and preventing financial crime.

In the event that there is any inconsistency between this Act and another financial sector law, this Act prevails. The Act applies to:

- 'Financial institutions' which includes product and service providers and persons licensed under financial sector law.
- 'Financial products' which includes a long-term insurance policy and benefits provided by retirement funds.
- 'Financial services' which includes giving advice and providing administration services.
- 'Financial stability' which refers to the ability of financial institutions to provide their services and products without interruption even if there are changes in economic circumstances.
- 'Financial sector law' which includes the Pension Funds Act and the Long Term Insurance Act.

New authorities created under the Act

A number of new authorities and committees have been established in the Act:

- Financial Stability Oversight Committee which provides support to the South African Reserve Bank. It is made up of representatives from the SARB, Government and other regulators.
- Financial System Council of Regulators which facilitates co-operation, consistency, and collaboration between various Government representatives and regulators.
- Financial Sector Conduct Authority (the FSCA) which is a market conduct regulator focusing on the fair treatment of customers and provides financial education. It replaces the Financial Services Board ("the FSB"). The FSCA has delegation authority and will regulate and supervise funds in accordance with this Act and the Pension Funds Act. The head of the FSCA will be known as the Commissioner and will be assisted by between 2 and 4 deputy Commissioners. The FSCA will publish its regulatory strategy, explaining what its regulatory and supervisory priorities are for the next 3 years and set out the guiding principles for how it will perform its functions.
- Financial Sector Contingency Forum which assists the Financial Stability Oversight Committee to identify systemic risks and the mitigation of these risks.
- Financial Sector Inter-Ministerial Council which facilitates co-operation between Cabinet Ministers responsible for legislation relating to the financial sector.
- Prudential Authority which is a juristic entity operating in the administration of the SARB. It promotes the safety and financial soundness of financial institutions and protects customers against the risk of financial failure of an institution.
- Prudential Committee which oversees the management and administration of the Prudential Authority.

Regulatory instruments

The Act sets out the procedure to be followed in issuing any new regulatory instruments. This includes a publication and consultation process. There is a separate process to follow if the regulatory instrument must be issued urgently, for example, where consumers are being prejudiced.

These instruments may deal with extensive topics, including fit and proper requirements, governance, and duties of key persons (such as trustees), operational requirements, financial management, record-keeping and data management, outsourcing, business continuity, conflicts of interest and safekeeping of assets.

This publication does not provide advice. If you have any questions/comments on the above, please contact your consultant.

Prudential standards

These are issued by the Prudential Authority (“the PA”) and relate to ensuring financial stability.

Conduct standards

These will be issued by the FSCA and can apply to financial institutions (funds) or key representatives (trustees).

The conduct standard can be aimed at ensuring the efficiency and integrity of financial markets; ensuring institutions and their representatives treat their customers fairly; ensuring financial literacy programmes are appropriate; reducing the risk of financial crime; and helping maintain financial stability.

A conduct standard can also declare a specific conduct to be an unfair business practice.

Joint standards

These are issued jointly by the PA and the FSCA.

Licensing

A person providing financial products and financial services must be licensed to do so. Where there is existing law regarding licensing, such as the Pension Funds Act ('the PFA'), that law will still apply unless the Act specifically overrides the PFA.

The Act deals with the process of applying for a licence and what happens if a licence is suspended or revoked. No licence may be issued, varied, suspended or revoked by one regulator without the agreement of the other regulator, namely the Prudential Authority (“PA”) and Financial Sector Conduct Authority (“FSCA”) going forward.

Inspections and investigations

The FSCA, which will be the regulator for funds and administrators, can make a written request for information or documents from funds and administrators. This request must be in respect of information which will assist the FSCA perform its functions or to assess risk of compliance or contraventions of the PFA.

On-site inspections may take place, with prior notification to the entity. The purpose of the inspection could be to assess compliance or contravention of applicable legislation. No one may intentionally or negligently interfere with an inspection.

The FSCA may appoint an investigator to carry out an investigation. The Act sets out the powers of investigators to question individuals and request the production of documents. A person who is answering questions or has to produce a document can refuse to do so, if they would incriminate themselves. Any questioning would be done under oath and a person being questioned is entitled to have a legal practitioner present to assist them.

Investigators can enter premises with prior consent or without prior consent or notification if they have a warrant to do so (it has to be issued by a Judge or Magistrate) or if the head of the FSCA believes a warrant would be issued and a delay would defeat the purpose of the search of the premises, they have the power to enter premises.

The Act sets out the conditions under which any search of the premises must be conducted. No one may intentionally or negligently interfere with an investigation.

Enforcement can be done in any of the following ways:

- Guidance notices may be issued by a regulator on the application of financial sector law (these are for information purposes and are not binding).
- Interpretation rulings are statements issued about the interpretation and application of financial sector laws. They aim to promote clarity, consistency, and certainty on the law. These rulings could be changed or withdrawn if the law changes or a court decides on another interpretation. These will be published for public comment before being finalized.
- Directives will require a financial institution or a key person at a financial institution to perform the action specified in the directive. This could happen where the institution is not treating its customers fairly or has or is likely to contravene the law. The directive could say that products or services should stop being provided, or the contravention must be remedied, or a person could be removed from their function in relation to the institution. This power applies in addition to the power to issue directives under the PFA.
- Enforceable undertakings are given by a person to the regulator about that person's future conduct in relation to the applicable financial sector law. If the regulator accepts the undertaking, then it is enforceable by the regulator. If the person then fails to comply with the undertaking, they could lose their licence. All undertakings will be published.
- Court proceedings can be instituted by a regulator to ensure compliance with any financial sector law. Any court order that is issued by the court will be published by the regulator.

- Debarment orders can be issued by a regulator against an individual who contravenes a local or foreign financial sector law or an enforceable undertaking or if they try to persuade someone else to contravene a financial sector law.
- Leniency agreements can be entered into where a person co-operates with an investigation. The extent of leniency will depend on the nature of the contravention, the extent of involvement in the contravention and the extent of co-operation.

Administrative penalties

Appropriate penalties can be imposed by a regulator against a person that contravenes a financial sector law or an enforceable undertaking.

The regulator will take the following into account in deciding what would be an appropriate penalty namely, the nature, seriousness and duration of the offence, the need to deter such conduct, the loss suffered by someone, if there is a prior offence, the extent of the benefit to the wrongdoer, the effect of the conduct and the penalty on financial stability and whether the conduct was deliberate or reckless. The penalty order will be published.

Unless the regulators allow it, no one can indemnify or compensate another person from having to pay an administrative penalty.

Fees and Levies

A regulator can charge fees and levies under this Act and the relevant financial sector laws to fund its activities. Fees and levies must be published. Different fees and levies can apply to different types of entities.

The regulator must provide every entity that has to pay a levy with an assessment of the levy that will be payable.

Sharing of information

Regulators, ombudsmen and state bodies may collect, use, share and disclose information, including personal information, to perform their duties under the Act and other relevant financial sector laws.

Regulators must liaise with one another and enter into agreements in respect of the co-ordination of reporting and sharing of information. Parties must be satisfied that the information they share will be safely stored by the receiving parties.

Offences and penalties

- An institution acting without a licence can receive a fine of up to R15 million or imprisonment of up to 10 years or both;
- An institution failing to report as required under the Act can receive a fine of R5,000 for every day the offence continues. The Act does not cap this amount.
- The failure to publish or disclose a licence can result in a penalty of R50,000.
- Not meeting the requirements of an inspection or investigation can result in a fine of between R1 million and R5million, depending on the offence and in some cases imprisonment.
- Non-compliance with an enforcement order can result in a fine of R15 million or imprisonment of up to 10 years or both.

Financial Sector Information Register

National Treasury will establish and maintain a Register to provide reliable electronic access to accurate, authoritative, and up to date information on financial sector laws. The public will be able to access this Register.

Ombud Council

The Ombud Council will ensure that financial customers have access to affordable, effective, independent and fair dispute resolution processes for complaints against financial institutions about their products or services.

The Council can issue directives, go to court, debar persons, issue administrative penalties, request information and perform inspections and investigations.

The Council will establish a call centre to assist customers in formulating complaints and identify the appropriate Ombud scheme for complaints.

Financial institutions cannot call their internal procedures an Ombud scheme. They must publicise the details of applicable Ombud schemes to customers.

Financial Services Tribunal

The Minister of Finance will appoint the Tribunal members, which will include two retired judges and two people with financial services experience (the Tribunal will replace the FSB Appeal Board). This Tribunal is established to reconsider decisions made by a regulator, the Ombud Council, a statutory Ombud or a licensed financial services provider.

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The decisions that can be reviewed by the Tribunal include the failure of a decision-maker to make a decision within a required or reasonable time period; or an act or omission following on from a decision made by a decision-maker.

The Act, sets out the time frames and procedures to be followed, to refer a decision to the Tribunal, including the right to receive reasons for any decision made by a decision-maker. The Tribunal can make the following orders namely, dismiss the application to reconsider the decision; or set aside the decision and ask the decision-maker to review their decision; or set aside the decision and the Tribunal can make a new decision.

The Tribunal's order can be made an order of court, in which case it has the same effect as a civil judgment. Any party that is unhappy with a Tribunal's decision can go to court to get the Tribunal's order reviewed.

Transition period

- The powers of the PA to ensure financial soundness will be delegated to the FSCA in respect of pension funds for a period of 3 years.
- The assets, liabilities and staff of the FSB will transfer to the FSCA.
- Inspections and investigations being undertaken by the FSB will be continued by the FSCA.
- The FSB Appeal Board and Enforcement Committee will cease to exist, once they finalise the matters they are currently busy with.
- In litigation underway involving the FSB, the FSCA will be substituted for the FSB.
- Licences in force before the Act will remain in force.

Changes to the Pension Funds Act

New definitions to be inserted into the PFA include:

- 'Authority' means the FSCA;
- Inserting a reference to the Act;
- Conduct standards, joint standards, prudential standards, Register and Tribunal.

The definitions of the 'FSB', 'prescribed' and 'Registrar' have been deleted. A new section 1A deals with the relationship between the PFA and the Act. Any reference to the registrar or FSB must be read as a reference to the Authority. The Authority will have powers under the PFA and the Act. Any notice to be published in a Government Gazette will also be published in the Register referred to above.

A fund could be financially unsound as determined in accordance with a prudential standard.

Housing loans issued by funds will be subject to prudential standards.

The FSCA may issue a directive to a fund requiring the rules relating to trustees to be amended in certain circumstances.

The Pension Funds Adjudicator ('the Adjudicator') will be a statutory Ombud. When dealing with complaints, the Adjudicator must take into account:

- where appropriate, principles of equity;
- contractual or legal relationships between a complainant and an institution;
- the Act.

