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FSCA STRATEGY FOR PROMOTING TRANSFORMATION IN THE FINANCIAL SECTOR

In case you missed it...

1. [January 2022: Recent Papers issued by National Treasury](#)
2. [February 2022: Budget summary 2022/23 Tax Year](#)

1. BACKGROUND

The Financial Sector Conduct Authority (“FSCA”) and other regulatory authorities have been concerned for some time that meaningful participation by the majority of South Africans in the financial sector is limited.

The FSCA’s strategy document aims to:

- outline the FSCA’s approach to promoting financial sector transformation within the existing policy framework, including the Financial Sector Regulation (“FSR”) Act, 2017, and
- outline an approach for the FSCA to promote transformation under the legislative framework which will be provided under the future Conduct of Financial Institutions (“COFI”) Act.

2. CURRENT POLICY AND LEGISLATIVE FRAMEWORK

The current policy and legislative framework include the following:

- One of the objectives of the FSR Act is to promote the transformation of the financial sector;
- The Financial Sector Code (“the FS Code”), as revised and gazetted in 2017,

seeks to promote the broad-based empowerment of black people by:

- increasing the number of black people that manage, own and control enterprises and productive assets in the financial sector;
- facilitating ownership and management of enterprises and productive assets by communities, workers, cooperatives and other collective enterprises;
- investing in the skills development and training of existing and new black professionals and managers;
- achieving equitable representation in all occupational categories and levels in the workforce;
- increasing empowerment financing; and
- increasing access to financial services.

- In relation to retirement funds, the FS Code introduced a “voluntary dispensation” of disclosure for the top 100 funds, including umbrella funds. In terms of voluntary disclosure, retirement funds are required to inter alia:

- Report annually on the proportion of fund liabilities attributable to black male and female members;
- Disclose details related to training of trustees and principal officers and initiatives to educate the membership;
- Report on their B-BBEE score achieved and on plans to improve that score.

- The Financial Sector Transformation Council (“FSTC”) was established under the enabling legislation of the B-BBEE Act, and contains several objectives aimed at promoting transformation of the financial sector, including engaging with financial institutions to facilitate understanding of and compliance with the FS Code. However, the FSTC is not mandated to take action against financial institutions in relation to the lack of achievement of targets of the FS Code, or failure to report on compliance.



Measures to promote transformation in terms of the current legislative framework are non-coercive and are based on engaging with stakeholders to encourage compliance. At present, there is no enabling legislation in the financial sector to enable the FSCA to play a direct role in relation to transformation.

However, if retirement funds fail to comply with the requirements specified under the FS code described above, the voluntary system may be revised.

3. THE FSCA STRATEGY

The strategy detailed in the document for comment is based on a two-phase approach. Phase 1 will be to promote transformation under the existing policy and legislative framework. Phase 2 will continue with the measures taken under Phase 1, but the enactment of the COFI Bill will create a new legislative framework for the FSCA to become more directly involved in enforcing compliance with transformation objectives.

3.1 Phase 1 – engaging with stakeholders and FSCA system development

The FSCA aims to achieve the following strategic objectives in Phase 1:

- Engaging with financial institutions on existing transformation plans and levels of compliance. This will involve the extent to which financial institutions are currently achieving their transformation targets and their compliance with the FS Code.
- The quality of available data is crucial for effective policy making and supervision. In November 2021, the FSCA issued FSCA Information Request 2 of 2021 in terms of which all Principal Officers of retirement funds were required to upload certain information onto the FSCA online system, including details of the racial composition of the board of trustees. So it is clear that the FSCA is already seeking to expand and update its current data on transformation in order to ensure it is equipped with reliable data to effectively monitor transformation in the financial sector and individual retirement funds going forwards. Data pertaining to the ownership structures of large organisations is often complex.

The FSCA will therefore undertake a data collection and clean-up exercise to strengthen and improve the information it holds regarding the ownership of licensed financial institutions.

- Co-operating with organisations such as the FSTC and the B-BBEE Commission, together with supporting initiatives of the National Economic Development and Labour Council (NEDLAC) which are related to transformation. These could include the convening of a second Financial Sector Summit to discuss issues related to transformation. The FSCA is already in the process of updating and revising the FS Code.
- Supporting small black-owned businesses in the Financial Sector. For some small businesses, the regulatory and supervisory requirements of the FSCA can be a barrier to entry and can even cause a business to fail due to the cost of complying with these requirements. The FSCA have proposed the development of regulatory and supervisory frameworks which will allow for proportional application of requirements in order to minimise barriers to entrance and compliance burdens for certain qualifying SME's.
- Training and up-skilling staff of the FSCA who are involved with licensing, supervisory and regulatory requirements in anticipation of Phase 2. The FSCA will then begin to consider the criteria that could be included for transformation to become a factor when issuing licenses to financial institutions, bearing in mind that all institutions, including retirement funds, will have to be licensed under COFI.
- Enforcement - the FSCA is currently able to take enforcement action against financial institutions that do not adhere to commitments made in terms of their transformation plans. However, at present an individual retirement fund is not required to submit a transformation plan.

3.2 Phase 2 – implementation of empowering legislation under COFI

3.2.1 Provisions in the COFI Bill

The COFI Bill imposes direct requirements on financial institutions regarding transformation, such as the requirement to have in place a transformation plan and to promote transformation

in line with that plan. The Bill intends to put in place a legislative framework that supports transformation.

Key proposals under the COFI Bill are as follows:

- Promoting transformation will be made an explicit function of the FSCA in terms of the FSR Act;
- Each financial institution will be required to promote transformation in a manner reasonably consistent with its transformation plan which itself should be aligned to tangible targets specified in the FS Code;
- The FSCA will now have the power to issue directives in relation to transformation plans and can use its enforcement powers if it has reason to believe that a financial institution’s governance framework does not adequately comply with transformation objectives or is not being adhered to.

3.2.2 How will the FSCA promote transformation under the new legislative framework?

The strategy document outlines the following actions which will place direct requirements on financial institutions relating to transformation and supervise compliance with these:

- All financial institutions with an annual revenue of over R10 million should have a B-BBEE Level 4 score or have a transformation plan in place which demonstrates how they will reach this level within 5 years. The regulatory and supervisory divisions of the FSCA will engage with non-compliant institutions. They will also engage with current B-BBEE level 4 institutions with a view to ascertaining whether they need to improve their transformation profile in any particular area. Ultimately, where there is non-compliance or transformation plans are inadequate, the FSCA have the power to issue an administrative penalty, an enforceable undertaking or a directive against the institution concerned.
- The FSCA mandate would be limited to enforcing financial sector laws only and not the B-BBEE Act or the FS Code, as these are the responsibility of the B-BBEE Commission and FSTC respectively.

However, the FSCA will engage actively with these institutions to support the work of these bodies. For example, the FSCA could support the B-BBEE Commission in an investigation of a particular financial institution.

- The requirements of the legislative framework established by COFI may be applied proportionally. This could mean that small and emerging black-owned businesses could be fully or partially exempted from some of the requirements of COFI and other regulatory requirements.

4. WHAT WILL BE THE EFFECT OF FSCA STRATEGY ON RETIREMENT FUNDS?

This is a strategy document, so it does not contain specific details, However, each retirement fund is a financial institution so the proposed legislation will apply to an individual retirement fund. Each retirement fund has to be licensed under COFI once it becomes legislation and it is likely that the FSCA will apply transformation criteria when considering applications for licenses. A retirement fund will have to have a transformation plan in place and aspects the FSCA may look at are:

- The composition of the board of trustees taking into account the racial profile of the membership;
- The B-BBEE rating of service providers to the fund;
- Does the fund support small black-owned enterprises in the financial sector, for example emerging investment houses?;
- Whether the fund’s investment policy statement is aligned to its transformation policy.

In general, once COFI is enacted, the FSCA are likely to make adherence to the requirements of the FS Code mandatory instead of voluntary and to extend its application beyond the top 100 funds. Further, the FSCA will be empowered to take a more inquisitorial and coercive approach in their supervision of retirement funds and their service providers, in particular with regard to whether these institutions are adhering to the transformation requirements under the COFI legislation.

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