



ASSOCIATED COMPLIANCE

FOR A COMMON PURPOSE

**Proposed Amendments of Fit and Proper requirements for
Financial Service Providers and Representatives**

Special Newsletter

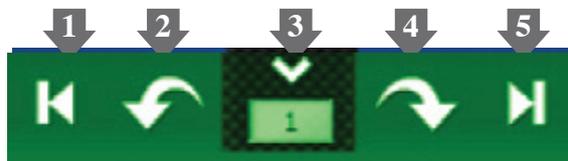
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Proposed Amendments of Fit and Proper requirements for Financial Service Providers and Representatives

We provided some initial input on these proposed changes in last month's newsletter. We have now fleshed this initial article out with more detail and commentary where appropriate.



Where indicated we intend providing input to the FSB by the stipulated deadline of 15 December 2016.

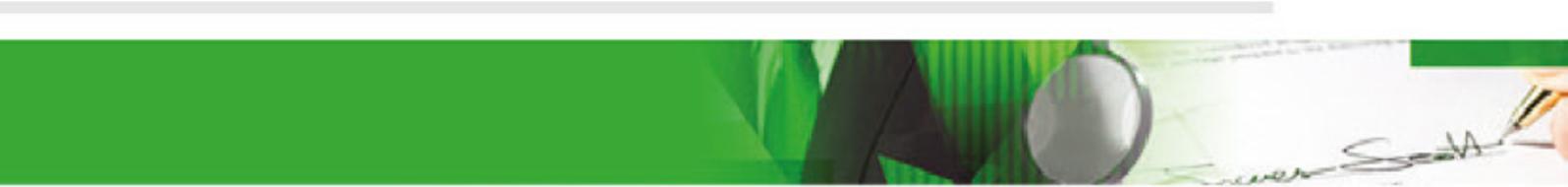
The proposed implementation date for these changes is 1 March 2017

There are three separate documents:

1. An explanatory memorandum on the proposed changes
2. The draft Board Notice itself
3. A summary of the Regulator's responses to the submissions made to the 2015 document.

[Click here](#) to download the explanatory memorandum and [here](#) for the draft Board Notice itself

There are 7 chapters.



Chapter 1:

Interpretation, Purpose and Application of this determination

Many of the included definitions support one or more the proposed amendments and we will deal with them as appropriate in the relevant Chapter review but some of the key ones to note are as follows;

- A new licence category for a “participatory interest in a hedge fund”
- A new licence category for a “structured deposit”;
 - a. Combination of a short term deposit or a long term deposit and another financial product
 - b. a short term deposit or long term deposit where the return or value is dependent on the performance of or is derived from the return or value of one or more underlying financial product, asset, rate or index, or a measure of economic value or on a default event
- Category B1A: a disability, health, life policy which require limited or no underwriting,
 - Category B2A: an investment policy with guarantees, disability, health or life policy with risk benefits with a guaranteed investment value or an annuity with a Rand based minimum value where the investment portfolio is managed by the product supplier with no option to amend that portfolio
 - Personal lines A1: a policy other than marine policies (although there is no definition in the Short-term Act of “marine”), engineering policies and guarantee policies;
 - that require no or limited underwriting (although the draft definition of limited underwriting does not deal with short-term risks),
 - define policy benefits as a sum insured and provide for the replacement of the asset or settlement of the balance of credit agreement debt,
 - are not subject to average,
 - have a term less than 24 months,
 - have limited exclusions.



We see this category being applicable to products such as cell phone insurance, motor warranty and “dent & scratch” covers

Overarching categorisation of products into either Tier 1 or Tier 2 and Classes (and related sub-classes) of Business both of which impact on the competency and CPD requirements which we will deal with later.

Tier 2 products are seen as being generally simpler and better understood than Tier 1 products. Tier 2 products include;

- Short term insurance personal lines A1
- Long term insurance sub category A, B1-A, B2-A,
- Friendly Society benefits
- Short and long term deposits

Class of Business: There are 7 classes of business with the first 5 having various Subclasses;

1. Short-term Insurance
2. Long-term Insurance
3. Retirement
4. Deposits
5. Securities & Investments
6. Forex Investments
7. Health Service Benefits

[Click here](#) to download the specific annexures that detail both the Tiered structure and class and subclass of business

- 
- To introduce the concept of “automated advice” which means; “furnishing of advice through an electronic medium that uses algorithms and technology without direct involvement of a natural person”

This also flows through into competency requirements.

- Definitions of personal and commercial lines: This clearly states that insurance purchased by “...natural persons acting in a business capacity” is commercial insurance. This may have the required impact in sectors such as motor where the lines between the two have long been blurred.
- Execution of sales: This is specific type of intermediary service that states “means an intermediary service performed by a person on instruction from a client that results in the conclusion of an agreement to buy, sell, deal, invest or disinvest in, replace or vary one or more financial products” This has a specific impact on the qualification, regulatory exam and CPD requirements.



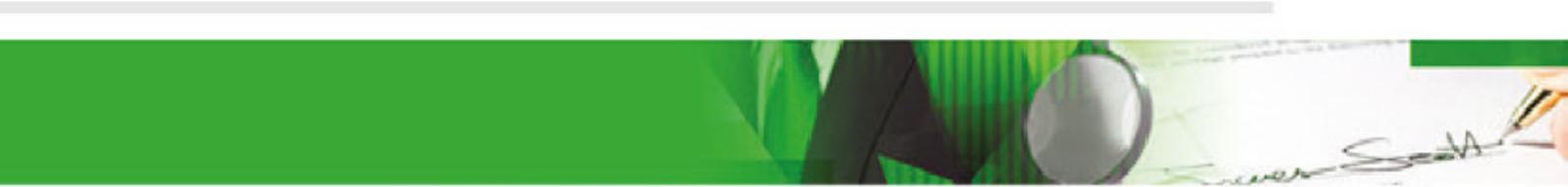
Chapter 2:

Honesty, Integrity and Good Standing

The heading of this Chapter has been amended from the current regulations of “personal character qualities of honesty and integrity” to that noted above. Generally the concept of “good standing” has taken a much higher profile in this draft than in the first draft from 2015 and has been extended to include specific reference that a juristic entity will demonstrate its compliance with the honesty, integrity and good standing “..through its corporate behaviour and through the personal behaviour of its directors and key individuals” This really brings in the “market conduct” focus that the regulator will be assuming in the near future and extends the net way beyond a simple rules based approach for nominated key individuals.

The meaning of good standing was questioned after the first draft was released and definitions requested to add structure to what was seen as a very wide term. The FSB disagreed and stated “...the meaning of good standing is a well-established principal” In our initial discussions with clients we don’t see that the “well established principal” is as established as the FSB believe it to be.

There is also an extensive list under 15 headings of “Incidents indicating when persons are not honest or lack integrity or good standing” These include, in addition to the expected theft, fraud and the like;



Where the person

- “has been subject to frequent or material preventative, remedial or enforcement actions by the registrar...”
- “has breached a fiduciary duty”
- Lost membership/designation of a professional body due to, amongst other things, integrity or business conduct (read ‘failure to achieve the CPD standards of the body’)
- Has been involved (director, trustee, member, controlling shareholder, managing executive) in a company that has gone into liquidation or placed under business rescue
- “has demonstrated a lack of readiness and willingness to comply with legal, regulatory or professional requirements and standards”

Many of these “incidents” include pending actions/events. When this aspect was questioned following the first draft the FSB responded that actual convictions, in the case of a criminal matter, is not a requirement for the regulator to take action. They also stated that the regulator would always take into account;

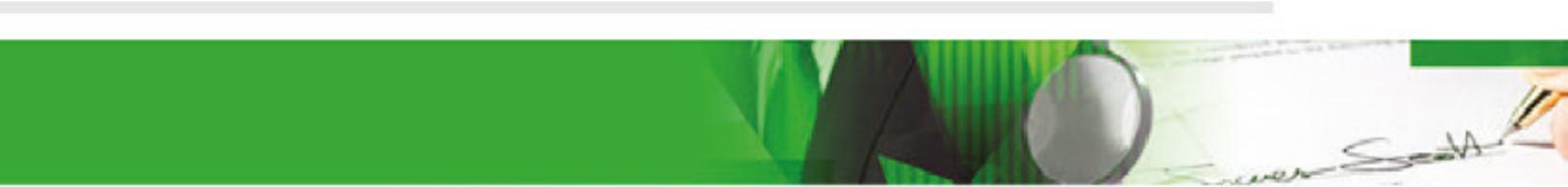
- The seriousness of a person’s conduct
- The relevance of such conduct or behaviour
- The passage of time since the occurrence.

And there would always be the option of an appeal against any decision but as we all know too well appeals can be lengthy drawn out matters and the impact on a person’s employment and/or business in that time could be serious.

We will certainly need to review and upgrade our recommended annual Fit & proper questionnaires as well as consider increasing the frequency of such checks to at least bi-annually.



The Representative supplementary application questionnaire that we recommend will also need to be expanded to cater for the proposed additional important criteria. In fact there are also proposed additional standards to be implemented for the recruitment of representatives (See details under Chapter 5) that amongst some new standards amongst other things replace the original proposal that dealt with a representative's inability to manage their personal financial obligations being seen as an automatic "fit & proper" issue.



Chapter 3: Competence requirements

This chapter is broken up into 5 parts;

Part 1: Application and general requirements

This section sets out the general responsibilities of an FSP in ensuring its Key Individuals and Representatives meet the various competence requirements that will demand that all current standards in this regard will need to be reviewed and upgraded.

One question for the FSB is the requirement that KI's and Representatives must be able to "...assess whether it is appropriate to offer a particular client and particular financial service..." which on the face of it would not be relevant to the UMA and/or FSP with a no advice model/product.

Another query for the FSB would be why the current requirement that an FSP must have at least one Key Individual per licence category that meets the same standards as demanded by a sole proprietor (but need not be appointed as a representative) seems to have been removed.

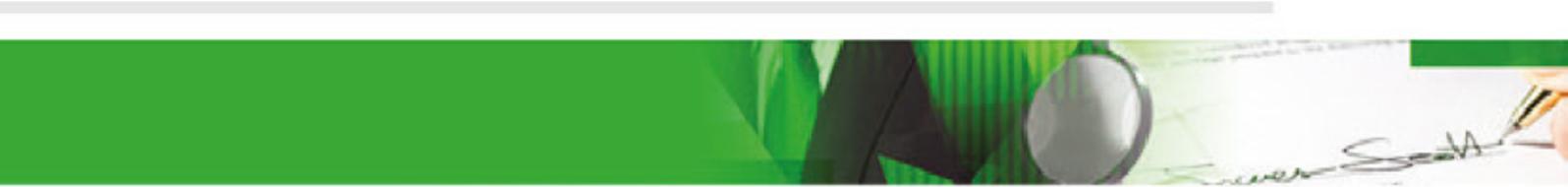
This section also sets out the minimum standards where "automated advice" is provided that effectively says that there needs to be at least one Key Individual that understands/has the experience of both the insurance and system technicalities utilised.



Part 2: Minimum Experience

In addition to setting the minimum experience requirements for Advice and Intermediary Services for the proposed licence categories ([Click here](#) to download the annexure for all category details) it deals with;

- General experience requirements, which are now stated to have to be “current”, presumably to tie in with the Continuous Professional Development standards
- Key Individuals need to have experience to manage per licence category being managed. The current standard that allows a general management Key Individual to be appointed is not addressed and will need to be queried with the FSB
- Lapsing of experience: This confirms the 5 year rule but makes it very specific that of the FSP, Key Individual or Representative has “not rendered” a service in a category for 5 consecutive years then the experience is deemed to have lapsed. As it is written and when read in conjunction with the “current” experience requirement such lapsing need not only occur when the representative status has been lost due to leaving the industry but can also be lost if simply a person does not actually act as a representative but has been left on a licence “for convenience” or “just in case” Such appointments will need to be reviewed.



Part 3: Minimum Qualifications

Restates the technical requirements for qualifications to be approved by the regulator. It also details who is exempt from having to obtain such qualifications, namely;

- Key Individuals and Representatives of a Category I FSP only licenced for;
 - Long Term Sub Category A
 - Friendly Society Benefits
- Representatives of a Category I FSP that is appointed only to perform the execution of sales in respect of a financial product subject to;
 - The representative has a Grade 12
- The execution of sales is performed;
 - In accordance with an approved (by KI & FSP) script
 - Under the direct oversight of a key individual who meets all the required standards in relation to the product concerned and is based at the same location where the execution of sales are performed

Plus other standards around checking advice is not provided and procedures and sales are monitored.

Whilst the focus on this is clearly the call centre agent they could apply equally to execution of sales done in, for example, retail stores but we do plan on seeking clarity on this aspect.

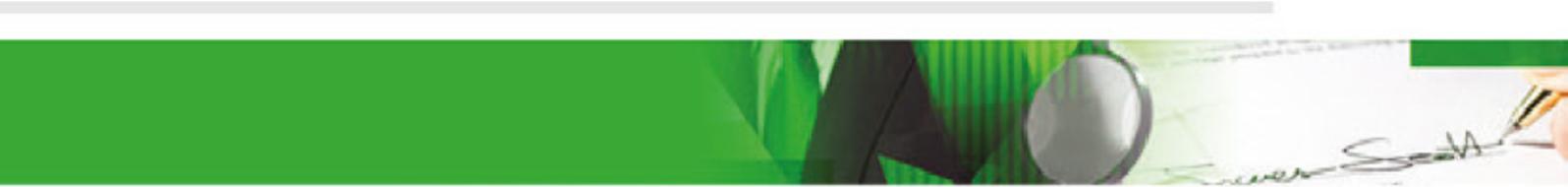


Part 4: Regulatory examinations

The need for what are currently referred to as the first level regulatory exams are retained. The originally proposed 2nd level exams have been dropped, although to be replaced with an alternative structure (see part 5 below)

There are provisions for lower standards as follows;

- Key Individuals and Representatives of a Category I FSP only licenced for;
 - Long Term Sub Category A
 - Friendly Society Benefits
- Representatives of a Category I FSP that is appointed only to perform the execution of sales in respect of a Tier 1 financial product and subject to the execution of sales being performed under the direct oversight of a key individual who meets all the required standards in relation to the product concerned and is based at the same location where the execution of sales are performed
- Representatives of a Category I FSP that is appointed only to perform a financial service in respect of a Tier 2 financial product



Part 5: Class of Business training and Product specific training

These proposals effectively replace the originally proposed 2nd level Regulatory exam. There are two components;

- Class of business training (generic knowledge relevant to a particular product and market or particular business sector) delivered by an accredited provider. This may well force employers and/or insurers/UMAs to seek accreditation to ensure training they provide meets the required standards. How feasible this accreditation process will be for smaller FSPs is not clear but the prospect of additional costs is likely.
- Product specific training (specialist or specific knowledge of a particular product). There is no requirement that this training be undertaken by an accredited provider and can be done in conjunction with class of business training. This training is not applicable to Category II, IIA and III FSP's

This training will **NOT** count towards CPD requirements. It is not clear if subsequent product training will be allowed as an accredited CPD event and will be taken up with the FSB

Whilst there are standards laid out there are no minimum hour or frequency standards set however both are subject to formal assessment i.e. a test.

The proposal also states that these levels of training must be provided "...prior to the rendering of any financial service..." and further that a Key Individual cannot "...manage or oversee.... unless (the KI) has completed the applicable class of business training and product specific training"

Whilst there are some built in exemptions and transitional arrangement (see below) the proposal does not deal with the practicalities of key individual and Representative movements within the industry in any way but it is assumed that once completed and proof is available then training done elsewhere will be acceptable by a new employer subject to proof that this knowledge has been kept "current" by the required CPD requirements having been completed.



It would of course always be subject to the FSP being satisfied that the Class of Business and product training originally completed is still relevant (In terms of Part 1 of this Chapter) It seems likely that both these basic levels of training will need to be refreshed on an on-going basis via the CPD process which is why we believe subsequent training done in this regard will be allowed for CPD purposes.

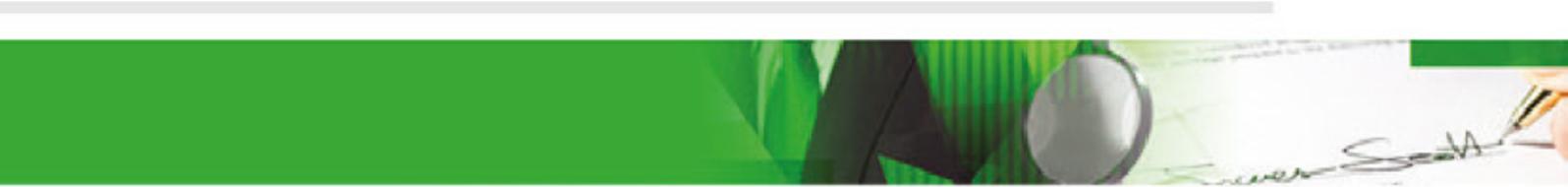
The exemptions to Class of Business training are;

- Key Individuals and Representatives of a Category I FSP only licenced for;
 - Long Term Sub Category A
 - Friendly Society Benefits
- Representatives of a Category I FSP that are appointed only to perform the execution of sales in respect of a Tier 1 financial product and subject to the execution of sales being performed under the direct oversight of a key individual who meets all the required standards in relation to the product concerned and is based at the same location where the execution of sales are performed
- Representatives of a Category I FSP that are appointed for Advice and/or Intermediary Services in respect of a Tier 2 financial product

The proposals do allow for a degree of “grandfather” clause in that;

- Key Individuals and Representatives (not under supervision) already appointed when the changes come into effect (Planned for March 2017) will be deemed competent on product specific training and any amended experience requirements.
- Key Individuals and Representatives (not under supervision) appointed prior to 1 January 2015 will be deemed competent for the class of business training. Those appointed from 1 January 2015 and any representative under supervision at the effective date of the changes (March 2017) will have 12 months to complete the required training.

These provisions will not apply should there be any changes to product or the market place that occur after March 2017 i.e. training will need to be provided, as it will on an on-going basis thereafter. Again clarity needed that such subsequent training will qualify for CPD recognition.



Obviously record keeping will be an essential part of this, and all other aspects, of the training and development of Key Individuals and Representatives. The FSB use the terms “competence register” in this regard and is something that we will be looking at more closely as we currently record much of the required data with your KI/Rep registers that are already set up to record CPD details.

Whilst not clearly set out as a requirement our initial thoughts are that each Key Individual/ Representative must take ownership of their own competency records (which will include CPD) so as to be able to quickly and easily provide them to an FSP (employer) or insurer or the regulator as and when required.



Chapter 4: Continuous Professional Development

Whilst most have a general understanding of what Continuous Professional Development (CPD) it will be important to really understand what the FSB say it is to ensure activities undertaken meet the required standards.

Let's start with what a CPD activity is;

- a. accredited and tracked by a Professional Body (e.g. IISA or FPI)
- b. allocated a hour value by that Professional Body and
- c. verifiable (i.e. you can prove it)

and excludes;

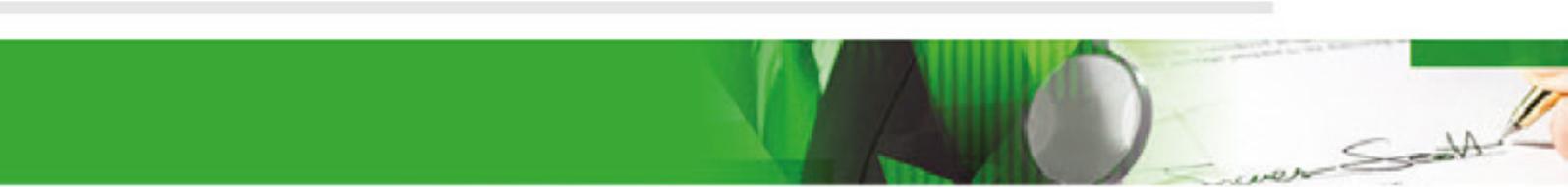
- i. an activity performed towards a qualification and
- ii. product specific training

We will be querying the “hour” rating along the lines of can you have an event that is less than 1 hour? And the previously noted issue around product specific training being excluded and our belief that this only refers to the compulsory product specific training and not any subsequent product based training.

The purpose of CPD within the above structure is, amongst other things, to;

- “maintain the required competency to render financial services...”
- “contribute to the skill, knowledge, expertise and professional and ethical standards of the FSP, Key Individual and representative”
- Identify any needs or gaps in the technical, generic or legal knowledge of the FSP, Key Individuals or Representatives
- Address any changes in both internal and external conditions in the market place and their products

These requirements will demand a formal and structured approach to ensure these requirements/needs are identified and plans made to address them and of course keep



the necessary records of what was done by whom for whom and when.

Each annual cycle will run from 1 June - 31 May each year. The hours to be achieved in will range from:

- Six hours where Key Individuals and Representatives are only licenced for one “sub class of business within a single class of business” e.g. Short-term would be a class and Commercial lines - engineering would be a sub class.
- 12 hours for more than one sub class within a single class e.g. Short-term and all sub classes of commercial business (engineering, motor, liability, and property).
- 18 hours where there is more than one class i.e. Short-term Personal and Commercial lines.

NB: See link in Chapter 1 to download the Class/subclass listing

CPD will not apply to:

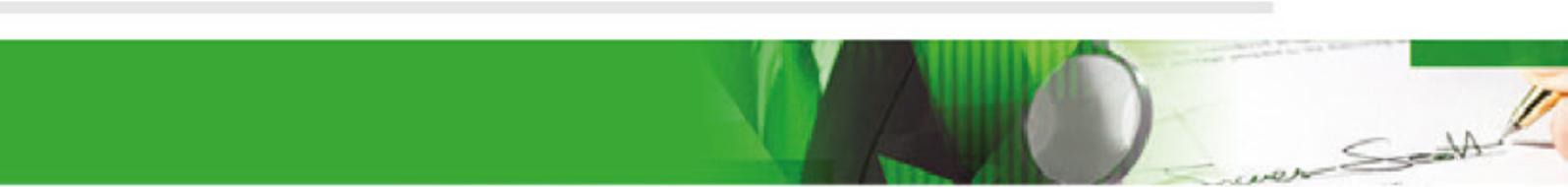
- Representatives only licenced for Funeral and Friendly Society benefits;
- Representatives of a Category I FSP only licenced for:
 - Advice in respect of Tier 2 financial product and/or
 - Intermediary services in respect of a financial product.(those FSP’s retaining Advice in their profile when not needed and/or used should now consider removing this to ‘avoid” a CPD requirement although our view is that the final version should have a CPD standard for intermediary services as these Key Individuals and Representatives still need to keep their knowledge and experience “current”



The proposals allow for pro rata hours when being appointed for the first time within a reporting cycle and where periods of absence from work due to maternity leave or extended sick leave or similar.

The role of the Professional Body will be a vital part of the process as they will not only approve all CPD activities but will also record and maintain all records of such activities at the individual and employer level and effectively means that everyone subject to CPD requirements will need to be a member of one of these bodies.

This will create a cost, which at this stage is not known. As to who pays this cost will be for the FSP to decide.



Chapter 5: Operational Ability

The current standards have been restated and substantially upgraded. The concept of proportionality (the controls and procedures should be proportionate to the “nature, scale and complexity of the business”) has been introduced. Whilst this allows a degree of logic to be applied to the rules the work involved in establishing and then justifying the proportionality applied has its own challenges.

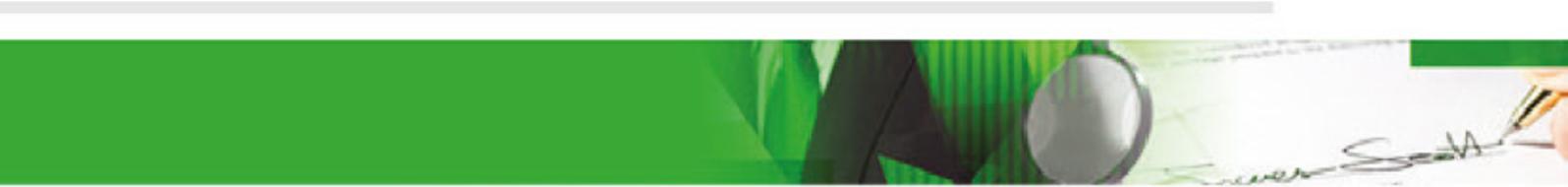
These changes will demand a review of all current policies and procedures, especially the risk management structures.

Interestingly the previous reference to the need for “guarantees or professional indemnity insurance or fidelity insurance cover” seems to have been omitted from this section. This will be queried but will probably be dealt with via a specific separate Board Notice given that the latest rules are dealt with by BN 123 of 2009.



Other key changes being introduced are;

- **Governance:** A governance framework, inclusive of a TCF policy and related procedures needs to be in place. The proposed regulations set out the minimum content of this framework. For many FSP's this will be uncharted waters. Is the launch of King IV recently something that will allow FSP's of all sizes to utilise in their adoption of this requirement?
- **Outsourcing of functions to persons other than Representatives.** Requirements on managing the outsourced function, which include functions that have to be done in a particular way to comply with FAIS or any other Act, and a function that is integral to the nature of the authorised financial services and any material important operational function of the FSP. This may well include a formal due diligence and on-going monitoring process and will definitely need a formal Service Level Agreement (as is the case already in such situations) Juristic representatives would fall into this section of control. The regulators desire to place firmer controls on key Individuals acting for more than one FSP are also built into these proposed regulations and will force all such Key Individuals to demonstrate, to the FSP's concerned, that they have the operational ability to perform their tasks for these various FSP's
- **The appointment of Representatives.** This will impact on the recruitment standards adopted by an FSP with a number of pre-employment screening processes to be undertaken e.g. financial history/status and for a juristic representative that they have the necessary operational ability.
- **Automated advice:** See definition in Chapter 1 above. Standards are being proposed that include;
 - The need for adequate and appropriate staff that have the required competence to manage and understand the technology and methodology
 - Specific policies and procedures for the technology that should, as a minimum, check the results being generated by the technology
 - Have adequate technological resources to maintain the records and data integrity



Chapter 6: Financial Soundness

The proposed amendments make it clear that;

- The requirements apply to all FSP's (other than registered banks and insurers)
- The requirements apply to Juristic representatives
- Being declared insolvent or placed under liquidation, including provisional status, will prevent an entity from obtaining and maintaining a licence.
- Being placed under business rescue will prevent an entity obtaining a licence or becoming a juristic representative
- An entity being unable to manage its own financial obligations – which includes being unable to provide satisfactory credit records (which of course means this aspect needs to be monitored)

The additional asset/solvency requirements currently in place remain but the definition of how liquid assets are calculated have been adjusted to allow them to be more practical. A requirement is to be introduced that demands a liquidity calculation to be undertaken. [Click here](#) to download the Draft format. This calculation will need to be submitted to the FSB each year with the financial statements for FSP's not handling client premiums/funds and twice a year to the FSB by Category II, IIA and III FSP's and twice a year by juristic representatives to their licence holder. AC will obviously update its own solvency calculation tool we currently utilise to match the new FSB standard where needed and continue to seek this each quarter. It is hoped the draft form referred to in the board Notice will be produced by the FSB in a pre-formatted excel spreadsheet so no errors can creep in when transposing numbers into a word/PDF document.

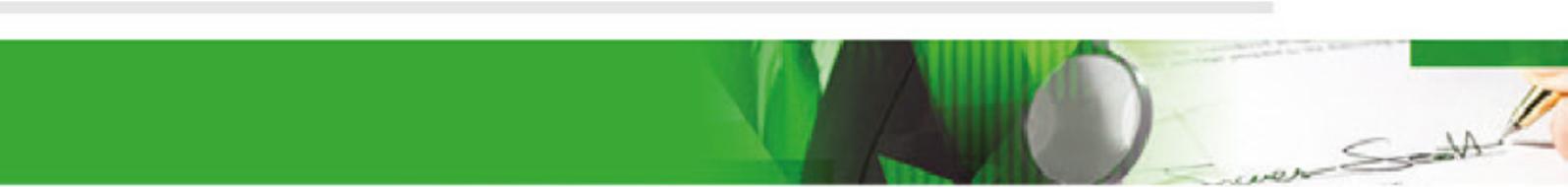
The concept of an early warning system is proposed. This applies to both the FSP and any appointed juristic representative.



This would demand an immediate report to the FSB when;

- An FSP that handles client funds/premiums has assets that exceed its liabilities by less than 10%
- An FSP that handles client funds/premiums has current assets that exceed its current liabilities by less than 10%
- A Category IIA or III FSP has its additional asset requirements exceeded by less than 10%
- None of the solvency requirements are met
- The FSP is aware that an event/situation may or will result in any of the above scenarios
- If and when any of the above occur "...the FSP may not make payments for loans, advances, a bonus, dividend, repayment of capital or other distribution of assets to any director, officer, partner, shareholder, related party or associate without the written approval of the Registrar" So, in simple terms if you know there is a problem you can't manipulate the situation for your own benefit

These standards will obviously demand far more scrutiny and possible reporting to the regulator, by ourselves going forward.



Chapter 7:

Repeals and Transitional provisions. The key transitional standards aspects have been dealt with insofar as they are appropriate, in the notes above.

The current regulations on exemptions for Supervision (Board Notice 104 of 2008) that would be applicable to Chapters 3 and 4 above will need to be dealt with by the FSB. In the feedback document from the 2015 draft the FSB did state that there was no need for the Board Notices dealing with the supervision standards to be repealed but will obviously need to be amended)

Conclusion

The above is merely a summary of the salient points of the proposed amendments.

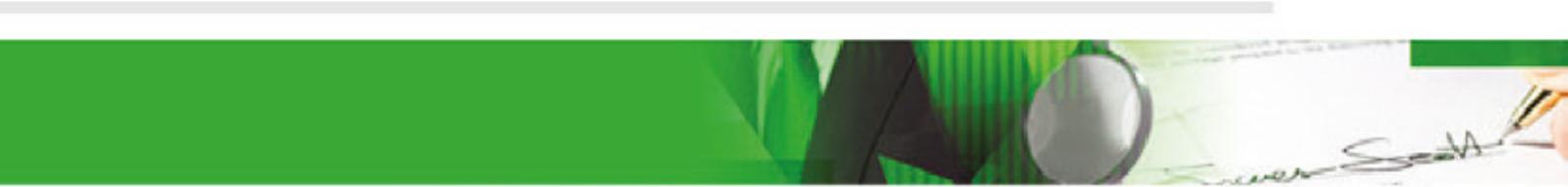
We expect that only the proposed replacement of the 2nd level regulatory exam and the CPD standards will provoke any real comment from industry given that the majority of the balance were in and commented on in the original December 2015 draft. As such the proposed



implementation date of 1 March 2017 is probably accurate, although the CPD is only likely to start from the proposed first full reporting cycle being 1 June 2017. These dates are further reinforced by the likely effective date of the Financial Sector Regulation Bill at 1 April 2017 that makes specific reference to these amended regulations.

We do intend providing our input to the FSB on the issues identified above and will gladly include any comments received from our clients on any of these proposals. Please submit all commentary to;

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