

Module # 1 – Component # 1



Regulatory Examinations Preparation FSPs (Sole Proprietors) and Key Individuals in Categories I, II, IIA, III & IV

Introduction to the FAIS Act

Tasks for this Course

1	Describe the role of the key individual in terms of the FAIS Act
2	Describe the role of the representative in terms of the FAIS Act.
3	Manage and oversee the appointment of representatives.
4	Manage the rendering of services under supervision.
5	Manage and oversee the ongoing development/employment of representatives.
6	Issue Debar representatives that have been found to act fraudulently, or committed any other act that gives rise to debarment.
7	Awareness of the regulatory environment in which the FSP functions.
8	Awareness of the specific obligations in terms of the relevant Code of Conduct and other subordinate legislation.
9	Oversee and manage the compliance functions as required by the FAIS Act.
10	Maintain the license of the FSP including the management of the licensing conditions.
11	Take the necessary action if the FSP voluntarily lapses its license
12	Verify that the proper record-keeping activities are carried out.
13	Manage and oversee/participate in the setting up and/or managing of the infrastructure of the FSP.
14	Manage and oversee the requirements that auditors/accounting officers must adhere to.
15	Manage and oversee the FSPs adherence to the requirements of FICA and other relevant anti-money laundering legislation, as it applies to the FSP.
16	Manage any processes required in the event of an investigation by the Ombud for Financial Services Providers (FAIS Ombud).

Glossary of Terms

Administrative Code: Board Notice 79 of 2003 on Codes of Conduct for Administrative and Discretionary FSPs (as amended).

Administrative FSP: This means an FSP, other than a discretionary FSP – (a) that renders intermediary services in respect of financial products referred to in paragraphs (a), (b), (c) (excluding any short-term insurance contract or policy referred to therein), (d) and (e), read with paragraphs (h), (i) and (j) of the definition of “financial product” in Section 1(1) of the Act, on the instructions of a client or another FSP and through the method of bulking; and (b) acting for that purpose specifically in accordance with the provisions of the Administrative Code, read with the Act, the General Code (where applicable), and any other applicable law.

Discretionary Code: Board Notice 79 of 2003 on Codes of Conduct for Administrative and Discretionary FSPs (as amended).

Discretionary FSP: This means an FSP - (a) that renders intermediary services of a discretionary nature as regards the choice of a particular financial product referred to in the definition of “administrative FSP” in this subsection, but without implementing any bulking; and (b) acting for that purpose specifically in accordance with the provisions of the Discretionary Code, read with the Act, the General Code (where applicable) and any other applicable law.

The FAIS Act: Financial Advisory and Intermediary Services Act, No. 37 of 2002.

Forex Code: Code of Conduct for Authorised Financial Services Providers and Representatives, involved in Forex Investment business.

FSB: Financial Services Board

FSP: Financial Services Provider

General Code: General Code of Conduct for Authorised Financial Services Providers and Representatives, (as amended).

Knowledge Criteria

- ☑ Describe the FAIS Act and requirements thereof (Part of Task 7)
- ☑ Explain the different financial products with examples of products in each category (Part of Task 10).
- ☑ Codes of Conduct (Part of Task 8)
- ☑ Explain the different financial products with examples of products in each category (Part of Task 10)

Introduction

The FAIS Act introduced market conduct legislation in South Africa.

It regulates the financial services market and became effective in 2002 with the main objective to protect consumers in relation to financial services with regard to the regulated products.

This topic provides an overview of the FAIS Act as well as the requirements and some key principles that will assist your understanding of the rest of the material.

The Purpose of the FAIS Act

1.1.1 Overview of the FAIS Act

The FAIS Act regulates the business of all financial service providers and intermediaries who give advice or provide intermediary services to clients.

The Act aims to professionalise the financial services industry and to provide adequate consumer protection.

The FAIS Act follows a functional approach and not an institutional approach. This means that the Act regulates certain functions across institutions (insurance companies, brokerages and banks). An institutional approach focuses on specific institutions, like the Banks Act for example, which regulates banks only. Therefore, the 'function' of providing financial services, across the various institutions, is governed by the FAIS Act.

Other examples of legislation that are applied across the whole financial services industry are: The Financial Intelligence Centre Act, 38 of 2001, The Financial Intelligence Centre Amendment Act, 11 of 2008 and The Companies Act, 61 of 1973.

The FAIS Act refers to the Financial Advisory & Intermediary Services Act, no. 37 of 2002. The commencement date of the FAIS Act is 15 November 2002, except for the following sections:

- ☑ Sections 20 to 31 became operational on 8 March 2003 (Proclamation 21 of 2003).
- ☑ Section 13(1) became operational on 30 September 2004.(Proclamation 35 of 2004)
- ☑ Section 7 became effective on 30 September 2004.(GN270/2004)

The FAIS Act has a number of role-players.

- ☑ The Financial Services Board (FSB) is an independent institution established by law to oversee the South African non-banking financial services industry in the public interest.
- ☑ Financial Services Providers (FSPs) are the financial institutions, insurance companies or other entities that need to be authorised or licensed by the FSB to provide financial services covered by the FAIS Act.
- ☑ Key individuals are employed by the FSPs and are responsible for the management and oversight of the FAIS-related business.
- ☑ Representatives are employed or mandated by FSPs to provide financial services to clients.
- ☑ Compliance officers are employed by or contracted by FSPs to assist in ensuring that the FSP complies with all the requirements of the Act.
- ☑ The Ombud for Financial Services Providers (FAIS Ombud) resolves disputes between consumers (clients) and financial service providers and their representatives with regard to financial services.

The Role of the Registrar's Duties and Powers in the FAIS Act

The FAIS Registrar is responsible for administration and enforcement of the Act, and the Registrar has defined functions, powers and obligations.

The FAIS Registrar authorises and issues licences to FSPs.

The form and manner of applications are stipulated in the Act as well as other authorisation requirements such as the fit and proper requirements.

The FAIS Registrar approves key individuals and compliance officers.

The subordinate legislation describes the fit and proper requirements.

The FAIS Registrar may publish Codes of Conduct.

The Codes describe the requirements when FSPs and representatives render financial services to clients.

The duties of FSPs are described in the Act and subordinate legislation.

There are specific provisions for compliance officers and compliance arrangements, requirements for record maintenance, disclosure, and auditing.

The FAIS Registrar has power to enforce the Act and to impose penalties.

The Act includes provisions relating to civil remedies, undesirable practices, offences and penalties, voluntary sequestration, winding-up and closure.

The Act describes the role and power of the Ombud for Financial Services Providers (FAIS Ombud).

Product Categories in the FAIS Act

1.3.1 The product categories in the FAIS Act

Each authorised FSP is licensed to provide financial services in relation to certain FAIS products. These products are defined and grouped in product categories.

FSPs may have various licences in respect of different product categories. The product category may also have different products falling in the main category and these are called product sub-categories.

The category descriptions in the FAIS Act are as follows:

“Category I”, in relation to a financial services provider, means all persons, other than persons referred to in Categories II, IIA, III and IV, who are authorised to render the financial services (other than financial services mentioned in Categories II, IIA, III and IV) as set out in the relevant application;

“Category II”, in relation to a financial services provider, means all persons who are authorised as discretionary FSPs as set out in the relevant application;

“Category IIA”, in relation to a financial services provider, means all persons who are authorised as hedge fund FSPs as set out in the relevant application;

“Category III”, in relation to a financial services provider, means all persons who are authorised as administrative FSPs as set out in the relevant application;

“Category IV”, in relation to a financial services provider, means all persons who require licences as Assistance Business FSP

The classification of the categories and sub-categories are important for the following reasons:

- ☑ FSP licences are issued for specific product categories
- ☑ Key individuals and representatives are approved and appointed to be operative within certain product categories and sub-categories
- ☑ Compliance officers are approved for certain product categories and sub-categories; and
- ☑ the fit and proper requirements relate to product Categories and sub-categories.

1.3.2 Examples of product sub-categories in the FAIS Act

Let's look at some examples of product categories and sub-categories:

CATEGORIES I: SUBCATEGORIES	
1.1	Long-term Insurance Subcategory A
1.2	Short-term Insurance Personal Lines
1.3	Long-term Insurance Subcategory B
1.3.1	Subcategory B1
1.3.2	Subcategory B2
1.4	Long-term Insurance Category C
1.5	Retail Pension Benefits
1.6	Short-term Insurance Commercial Lines
1.7	Pension Fund Benefits
1.8	Securities and instruments: Shares
1.9	Securities and Instruments: Debentures and securitised debt
1.10	Securities and Instruments: Warrants, certificates and other
1.11	Instruments acknowledging debt Securities and Instruments: Bonds
1.12	Securities and Instruments: Derivative instruments excluding warrants
1.13	Participatory interests in one or more collective investment schemes
1.14	Forex Investment Business
1.15	Health Service Benefits
1.16	Long-term Deposits
1.17	Short-term Deposits
1.18	Friendly Society Benefits

Please note that the Category I table was changed to 20 sub-categories in Board Notice 135 of 2012. Sub-category 1.3 is now Long-term Insurance Subcategory B1, with sub-category 1.20 Long-term Insurance Subcategory B2.

CATEGORY II: SUBCATEGORIES	
2.1	Long-term Insurance
2.1.1	Subcategory B1
2.1.2	Subcategory B2
2.2	Long-term Insurance Category C
2.3	Retail Pension Benefits
2.4	Pension Fund Benefits
2.5	Securities and instruments: Shares
2.6	Securities and Instruments: Money market instruments
2.7	Securities and Instruments: Debentures and securitised debt
2.8	Securities and Instruments: Warrants, certificates and other instruments acknowledging debt
2.9	Securities and Instruments: Bonds
2.10	Securities and Instruments: Derivative instruments excluding warrants
2.11	Participatory Interests in one or more collective investment schemes
2.12	Forex Investment Business
2.13	Long-term Deposits
2.14	Short-term Deposits

Please note that the Category II and IIA table was amended in Board Notice 135 of 2012 to include 16 sub-categories, with subcategory 2.1 being Long-term sub-category B1, sub-category 15 being Category II Hedge Fund FSPs and sub-category 16 being Long-term sub-category B2.

Codes of Conduct

As mentioned above, the FAIS Registrar may publish Codes of Conduct. The purpose of the Codes is to provide more detailed provisions regarding the rendering of financial services. These Codes are part of the subordinate legislation and are binding on all FSPs, key individuals and representatives.

Section 16 of the FAIS Act requires that the Codes must contain (at least) provisions relating to:

- ☒ making adequate disclosures
- ☒ adequate record-keeping
- ☒ avoidance of fraudulent and misleading advertising, canvassing and marketing
- ☒ proper safe-keeping, separation and protection of funds and transaction documentation of clients
- ☒ where appropriate, suitable guarantees or professional indemnity or fidelity insurance cover, and mechanisms for adjustments of such guarantees or cover by the registrar in any particular case the control or prohibition of incentives given or accepted by a provider; and
- ☒ any other matter which is necessary or expedient to be regulated in such code for the better achievement of the objects of the Act.

The following Codes have been published so far:

- ☒ General Code of Conduct for Authorised Financial Services Providers and Representatives, (as amended)
- ☒ Specific Code of Conduct for Authorised Financial Services Providers and Representatives conducting Short-term Deposit Business
- ☒ Code of Conduct for Authorised Financial Services Providers and Representatives, involved in Forex Investment Business
- ☒ Notice on Codes of Conduct for Administrative and Discretionary FSPs (as amended).

As and when required, the Codes are amended through the publication of Board Notices in Government Gazettes.

Types of Financial Services and Products

1.5.1 Types of financial services

To provide a financial service means to:

- ☒ give advice; or
- ☒ provide an intermediary service; or
- ☒ give advice and provide an intermediary service.

We refer to financial service throughout the material and it is important that you understand that it may consist of both or either of the above elements.

Sometimes a representative or FSP may only be authorised to give advice in respect of certain product categories, or to provide an intermediary service (without advice).

1.5.2 Advice

The FAIS Act defines 'advice' as follows:

Definition of advice:

"'advice' means, subject to subsection (3)(a), any recommendation, guidance or proposal of a financial nature furnished, by any means or medium, to any client or group of clients -

- a)** in respect of the purchase of any financial product; or
- b)** in respect of the investment in any financial product; or
- c)** on the conclusion of any other transaction, including a loan or cession, aimed at the incurring of any liability or the acquisition of any right or benefit in respect of any financial product; or
- d)** on the variation of any term or condition applying to a financial product, on the replacement of any such product, or on the termination of any purchase of or investment in any such product, and irrespective of whether or not such advice -
 - i.** is furnished in the course of or incidental to financial planning in connection with the affairs of the client; or
 - ii.** results in any such purchase, investment, transaction, variation, replacement or termination, as the case may be, being effected;"

Subsection 3(a) says the following:

Exclusions from "advice"

"a) advice does not include -

(i) factual advice given merely -

- ☒ on the procedure for entering into a transaction in respect of any financial product;
- ☒ in relation to the description of a financial product;
- ☒ in answer to routine administrative queries;
- ☒ in the form of objective information about a particular financial product; or
- ☒ by the display or distribution of promotional material:

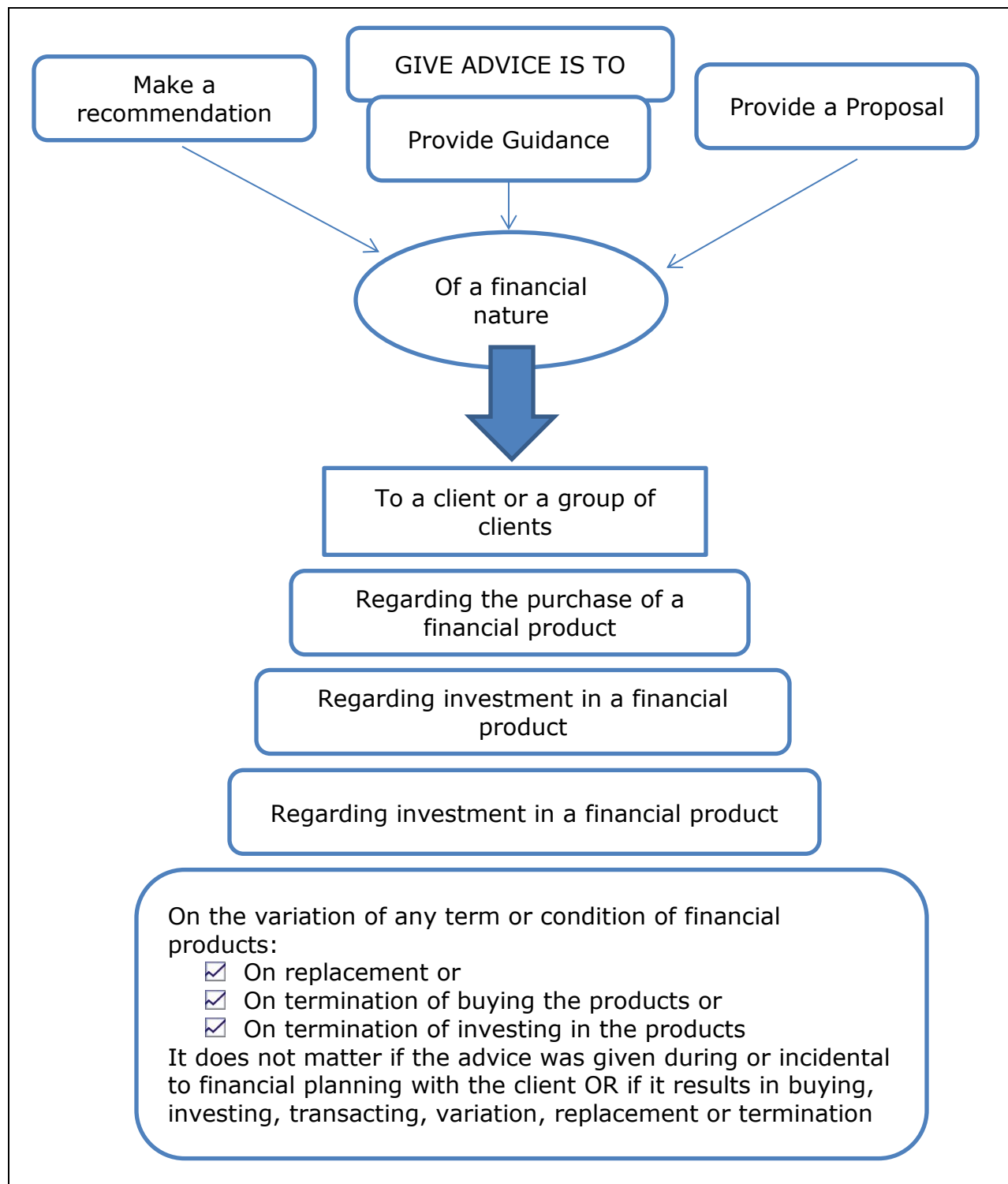
(ii) an analysis or report on a financial product without any express or implied recommendation, guidance or proposal that any particular transaction in respect of the product is appropriate to the particular investment objectives, financial situation or particular needs of a client;

(iii) advice given by -

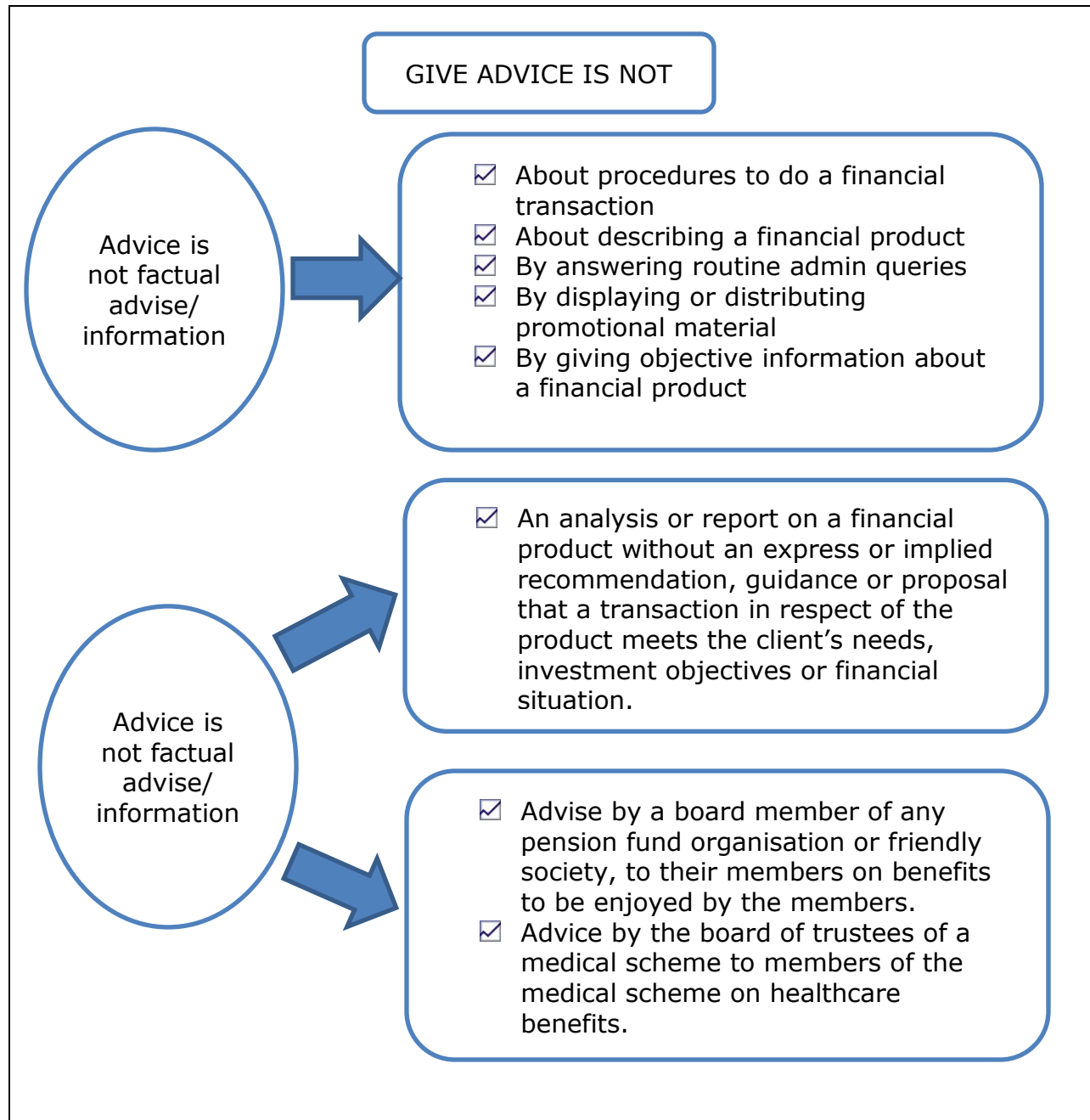
- ☒ the board of management, or any board member, of any pension fund organisation or friendly society referred to in paragraph (d) of the definition of "financial product" in subsection (1) to the members of the organisation or society on benefits enjoyed or to be enjoyed by such members; or
- ☒ the board of trustees of any medical scheme referred to in paragraph (g) of the said definition of "financial product", or any board member, to the members of the medical scheme, on health care benefits enjoyed or to be enjoyed by such members; or

(iv) any other advisory activity exempted from the provisions of this Act by the registrar, after consultation with the Advisory Committee, by notice in the Gazette;"

The elements of 'advice' include the following:



The following is not included in the definition of 'advice':



1.5.3 Intermediary service

Let's look at the elements of 'intermediary service' in order to distinguish between the two components which make up 'financial service'.

The FAIS Act defines 'intermediary service' as follows:

Definition of intermediary service:

"'intermediary service' means subject to subsection (3)(b), any act other than the furnishing of advice, performed by a person for or on behalf of a client or product supplier –

a) the result of which is that a client may enter into, offers to enter into or enters into any transaction in respect of a financial product with a product supplier; or

b) with a view to –

(i) buying, selling or otherwise dealing in (whether on a discretionary or non-discretionary basis), managing, administering, keeping in safe custody, maintaining or servicing a financial product purchased by a client from a product supplier or in which the client has invested;

(ii) collecting or accounting for premiums or other moneys payable by the client to a product supplier in respect of a financial product; or

(iii) receiving, submitting or processing the claims of a client against a product supplier;"

Exclusions from intermediary service

"b) intermediary service does not include –

(i) the rendering by a bank, mutual bank or co-operative bank of a service contemplated in paragraph (b)(ii) of the definition of 'intermediary service' where the bank, mutual bank or co-operative bank acts merely as a conduit between a client and another product supplier;

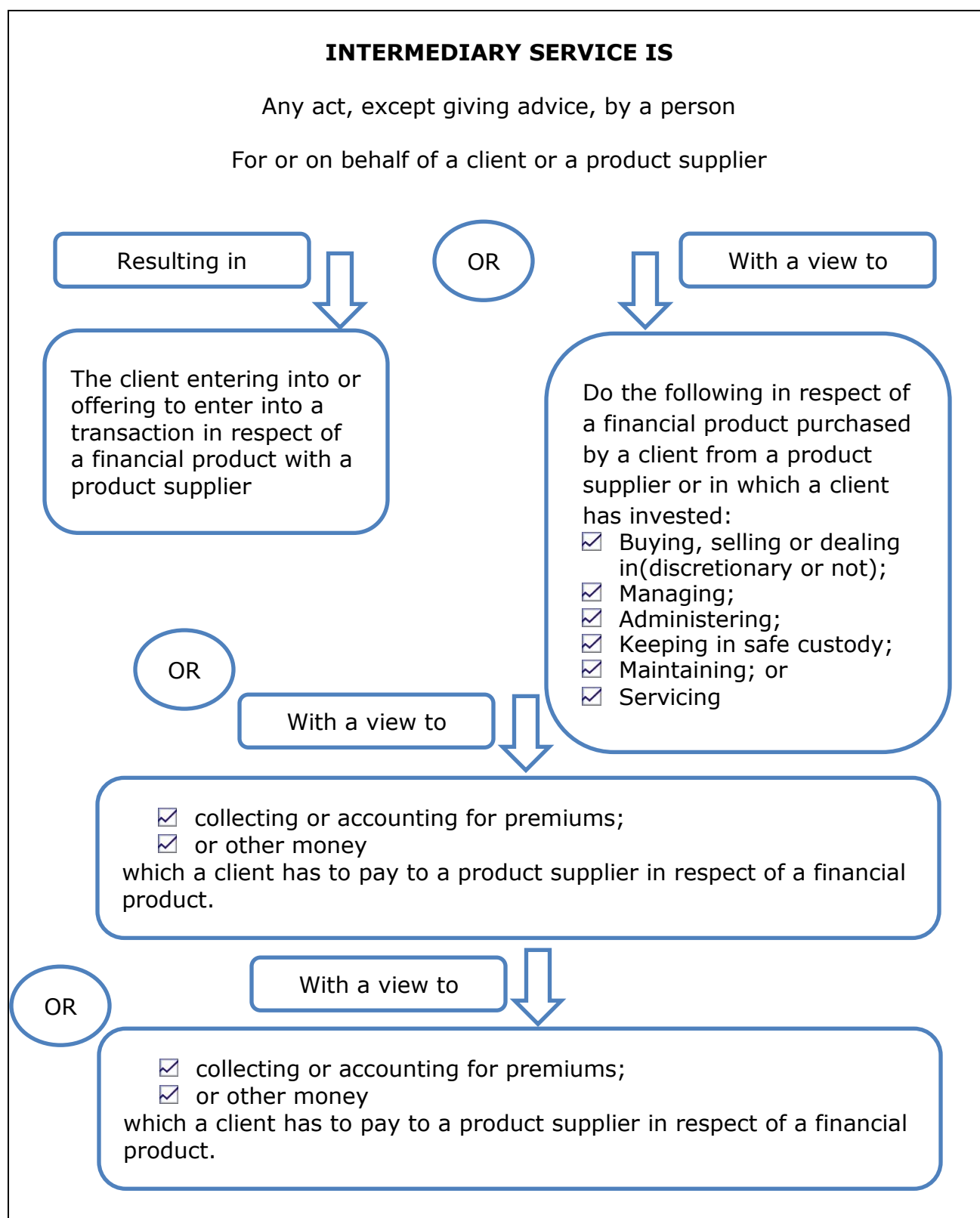
(ii) an intermediary service rendered by a product supplier –

☒ who is authorised under a particular law to conduct business as a financial institution; and

☒ where the rendering of such service is regulated by or under such law;

(iii) any other service exempted from the provisions of this Act by the registrar, after consultation with the Advisory Committee, by notice in the Gazette."

The elements of 'intermediary service' include the following:



1.5.4 Types of financial products

Financial products are grouped in the various product categories and sub-categories.

Below examples of financial products:

Financial product	Example
a) Securities and instruments, including: <ul style="list-style-type: none"> i. shares in a company other than a “share block company” as defined in the Share Blocks Control Act, 1980 (Act No. 59 of 1980); <ul style="list-style-type: none"> <input checked="" type="checkbox"/> debentures and securitised debt; <input checked="" type="checkbox"/> any money-market instrument. <input checked="" type="checkbox"/> any warrant, certificate, and other instrument acknowledging, conferring or creating rights to subscribe to, acquire, dispose of, or convert securities and Instruments referred to in subparagraphs (i), (ii) and (iii); <input checked="" type="checkbox"/> any “securities” as defined in Section 1 of the Securities Services Act, 2002. 	<p>Shares in a company such as Absa bank.</p> <p>An example of a debenture is an unsecured bond. Money market instruments are short-term financial instruments such as bankers’ acceptances, certificates of deposit.</p> <p>Securities include shares, stocks and depository receipts in public companies.</p>
b) A participatory interest in one or more collective investment schemes	Money market funds managed by a fund manager
c) A long-term or a short-term insurance contract or policy, referred to in the Long-Term Insurance Act (Act No 52 of 1998), and the Short-Term Insurance Act (Act No. 53 of 1998), respectively.	Credit life insurance as an example of Long-Term Insurance Category B
d) A benefit provided by: <ul style="list-style-type: none"> i. A pension fund organisation as defined in Section 1 (1) of the Pension Funds Act, 1956 (Act number 24 of 1956), to the members of the organisation by virtue of membership; or ii. a friendly society referred to in the Friendly Societies Act (Act No. 25 of 1956), to the members of the society by virtue of membership. 	Benefits include pay-out of money accumulated in a pension fund, for the benefit of the members
e) A foreign currency denominated investment instrument, including a foreign currency deposit.	
f) A deposit as defined in Section 1 (1) of the Banks Act.(Act No 94 of 1990)	Savings and 23-day notice deposit accounts.
g) A health service benefit provided by a medical scheme as defined in Section 1 (1) of the Medical Schemes Act (Act No. 131 of 1998)	Health benefits that are available in terms of a medical scheme

Summary

Topic 1 introduced you to the main purpose and ambit of the FAIS Act, which sets out to regulate financial services in South Africa.

We also discussed the product categories and sub-categories.

The categorisation of products is important because it is used for the following:

- ☑ FSP licences are issued for specific product categories.
- ☑ Key individuals and representatives are approved and appointed to operate within certain product categories and sub-categories.
- ☑ Compliance officers are approved for certain product categories and sub-categories.
- ☑ The fit and proper requirements relate to product categories and sub-categories.

The FAIS Act makes provision for Codes of Conduct. The Codes give us the detailed provisions that prescribe what and how to do things.

We also unpacked the concept of 'financial service' in this topic. Two elements make up 'financial service':

- ☑ advice
- ☑ intermediary services
- ☑ or a combination of both.

Only those financial products that are listed in the FAIS Act are subject to the Act.