



Financial Sector
Conduct Authority



Board Conflicts and FSCA Directive 8

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Legal Framework: Board Conflicts & Directive 8

1. What conflicts of interest must a board member and principal officer avoid?

Section 7C of the Pension Funds Act, 24 of 1956 (“the Act”) provides that:

“(2) In pursuing its object the board shall –

(c) avoid conflicts of interest.”

- **Background to Directive PF No. 8 of 2018**

- On-site inspections by the FSCA revealed that Service Providers were wining and dining board members and Principal Officers (POs) (paying for golf days, overseas trips, sports events, jazz festivals, etc).
- Cases further revealed that POs who were in the employ of Service Providers to funds were reluctant/failed to blow the whistle on them.

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- ❖ compromised their independence and made them beholden to their employer as opposed to acting in the best interest of the fund (fiduciary duty).
- Even though this was not a reflection of the entire industry, the number of cases were large enough to warrant concern and intervention.
- Directive 8 was therefore a response to the litany of abuse that had been observed and occurred in the retirement funds industry. It was evident that controls needed to be put in place.
- **Directive PF No. 8 of 2018**
 - Issued 8 March 2018
 - Prescribes conditions to combat and prevent corruption and corrupt activities in the retirement funds industry.

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- Defines gratification and specifies the types of gratification, which are impermissible.
- Places a reporting obligation on, *inter alia*, board members and POs of retirement funds.
- Paragraph 1(4) defines gratification as, *inter alia*,
 - (a) money, whether in cash or otherwise;
 - (b) any donation, gift, loan, fee, reward, security, property / interest in property or similar advantage;
 - (c) the avoidance of a loss, liability, penalty, forfeiture, punishment or other disadvantage;
 - (d) any office, status, honour, *employment, contract of employment or services*, any agreement to give employment or render services in any capacity and residential or holiday accommodation;

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...

(j) any valuable consideration or benefit of any kind, including any discount, commission, rebate, bonus, deduction or percentage (Prevention and Combatting of Corrupt Activities Act, 12 of 2004 (PRECCA))

but excludes remuneration paid by a sponsor of a retirement fund to a board member appointed by a sponsor of a retirement fund.

➤ General Principle – Board members and POs, *inter alia*, of retirement funds should not be involved in any conduct constituting corruption or corrupt activities. Any such involvement will have a bearing on such persons' fitness and propriety to hold office and/or to provide a service.

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- ❖ Corruption is defined as unduly influencing someone to act in a certain way, an abuse of power, to achieve an unjust outcome (section 3 of PRECCA).
- ❖ Corrupt Activities include bribery, fraud, anti-competitive behaviour, etc. (Part 2 of Chapter 2 of PRECCA).
- Paragraph 4(1)(a) provides, *inter alia*, that board members and POs are not permitted to accept any gratification, which objectively viewed creates a conflict of interest with their fiduciary duty towards the fund in which they serve.
- It is therefore evident from paragraph 1(4)(d) read with 4(1)(a) of Directive 8 that POs are not permitted to accept gratification, be it employment or a contract of employment, from a service provider to the fund.

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- **Further prohibits**
 - Board members and POs from receiving gifts exceeding the limit set in the fund's gifts policy (paragraph 4(1)(b))
 - ❖ But it may not be more than R500.
 - Receipt of any gratification related to international and local due diligences (paragraph 4(1)(c)).
 - Receipt of any gratification related to local or international entertainment or sporting event (paragraph 4(1)(d)).
 - Conferencing costs and board expenses (paragraph 4(1)(e)).



Directive 8: Clarifications

- **Communication 7 of 2019**
 - Issued:
 - ❖ 12 December 2019
 - ❖ against the backdrop of industry's request for clarity around whether the appointment of POs, who are in the employ of Service Providers, constitutes a conflict of interest.
 - Reiterated POs legal duty to protect members of the fund by reporting to the Authority any matter that may prejudice members of the fund
 - ❖ including reporting conduct of board members and Service Providers where they act in a manner that prejudices members of funds



Directive 8: Clarifications

- **Communication 7 of 2019 cont.**
 - Indicated that given the role of a PO s/he owes a fiduciary duty to the fund and should therefore avoid conflicts of interest.
 - Reiterated that Directive 8 prohibits POs from accepting any gratification including being in the employment of service providers (paragraph 1(4)(d) read with 4(1)(a) of Directive 8).
 - Outlined the steps the Authority would take against recalcitrant funds.
 - Provided 6-month compliance period.





Directive 8: Clarifications

- **Communication 47 of 2020**

- Issued:

- ❖ 21 August 2020

- ❖ to provide further clarification to the industry on the FSCA's position in respect of conflicts of interest relating to POs appointed whilst in the employ of service providers.

- ❖ to address concerns raised around the legal validity of Directive 8 insofar as it accords

- ✓ fiduciary duties to POs, and

- ✓ in that it precludes POs from being in the employ of service providers and/or sponsors to funds



Directive 8: Clarifications

Communication 47 of 2020 cont.

- The FSCA has always taken the view that a PO owes a fiduciary duty to a fund to act in its best interest.
- It has further taken the view that a PO of a fund may not simultaneously be in the employ of a service provider to the fund as this constitutes a conflict of interest.
- These views found expression and legal force in Directive 8.
- The advice provided by a respected Senior Counsel confirmed FSCA's views and confirmed the legal validity of Directive 8.

Directive 8: Way Forward

- Directive 8 is likely to be transposed to a Conduct Standard incorporating the clarity provided in the Communique.
- It may form part of the Governance Conduct Standard.

Directive 8: Alternatives?

3. Are there better ways of resolving these issues?

- In order to answer this question, we need to ask ourselves whether Directive 8 is yielding the desired results.
- As the Regulator, the FSCA is of the view that it has engendered a greater focus on good governance as the PO acts as a check on the Board, considering also the number of active funds in the industry.
- The FSCA has observed a greater level of compliance – more POs have come forward as whistleblowers. The FSCA welcomes this!
- In short, the FSCA's view is that Directive 8 is working and we will therefore not be looking at repealing any portions of Directive 8.

Directive 8: Alternatives?

- If anything, we would like to see the bolstering of good governance
 - Amended section 8 of the consequential amendments to COFI
 - Governance Conduct Standard
 - Fit and Proper Conduct Standard (across financial institutions pursuant to COFI)
 - Trustee Toolkit training is already compulsory (Conduct Standard 4 of 2020)
 - ❖ which ought to equip trustees with a basic understanding of good governance of funds; and
 - ❖ it is being enhanced and will provide more comprehensive training to assist board members to perform their duties more effectively.

THANK YOU