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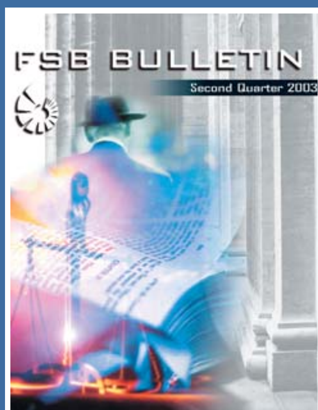

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Registrar of Pension Funds challenges Pepkor Limited in court – and wins again

The saga of the Pepkor Pension Fund took a turn for the better when the FSB and the Registrar of Pension Funds won a more generous dispensation for former members in court. Dr Elmarie de la Rey, FSB's senior manager: Legal, puts the case in perspective.

When the Registrar of Pension Funds in March 1994 granted the Pepkor Pension Fund certificates in terms of section 14(1) of the Pension Funds Act, 1956, for the transfer of business, the Registrar did not realise that a chain of events had been set in motion that would only be resolved many years later in the Supreme Court of Appeal (SCA). Soon after, it also became apparent that some R9,2 million was transferred from the Fund to the Pepkor Retirement Fund (the executives' fund), without authorisation.

The latter Fund was set up for a selected few executives of the Pepkor Group, not all of whom were former members of the Pepkor Fund, but who all stood to gain from the R9,2 million windfall.

In 1997, the FSB and the Registrar of Pension Funds took the Pepkor Pension Fund, Pepkor Limited and the retirement funds of certain subsidiaries to court to get a more generous dispensation for former members of the Pepkor Pension Fund.

After the Cape High Court granted an order in favour of the FSB and the Registrar, the executives' fund and Pepkor Limited lodged an appeal to the SCA in May 2003, where, with the exception of a minor point described by the court as being of academic interest only, the appeal was dismissed. As a result Pepkor Limited and the executives' fund will have to pay the substantial legal costs incurred by the FSB and the Registrar.

The appeal also resulted in new law being pronounced. Hitherto our courts have not permitted a review of an administrative decision, such as the approval of a section 14 transfer, solely on the basis of a material mistake of fact by the person who made the decision.

The SCA extended this principle and found that the FSB and Registrar were not only entitled, but in fact duty bound to raise the matter in a court of law, if prejudiced. In this instance the court found that the Registrar had been prejudiced.

To understand the judgment it is necessary to look at the history of the Pepkor Pension Fund (the Fund).

The Fund was a defined benefit fund registered in 1973 to provide retirement and other benefits to eligible employees in what was to become the Pepkor Group. The Group consisted of the holding company, Pepkor Limited, and three other operating companies: Ackermans, Pep Stores and Shoprite. During the mid 1990's the Fund was 'unbundled' – initially into three 'daughter' funds, the Shoprite Pension Fund, the Ackermans Pension Fund and the Pep Stores Pension Fund, which were also defined benefit funds; and ultimately, also into four defined contribution provident funds, the Shoprite Checkers Retirement Fund, the Ackermans Retirement Fund, the Pepkor Retirement Fund and the Pep Retirement Fund. The Fund continued to exist. The 'unbundling' was effected by a series of applications for transfers of business in terms of section 14(1) of the Act, all of which, except for the payment of the amount of R9,2m to the first appellant, Pepkor Retirement Fund, were approved by the Registrar. The Registrar granted approval for the transfers based on information provided to him by Mr EC Meyer, actuary or valuator to the Fund, on the funding level of the Fund - the ratio of the actuarial value of assets to the actuarial value of liabilities.

According to Meyer the funding level of the Fund before and after the transfers to the 'daughter' funds was 137%, with the exclusion of "special reserves." However, it was common cause that in fact the Fund's funding level before the transfers was 151% and thereafter, 606%. The Cape Court criticised Meyer's method of calculating the funding levels, which essentially involved the unwarranted exclusion of amounts in the Fund, as 'arbitrary and indefensible'.

The judge found that no attempt had been made to justify Meyer's calculations. The applications for the transfers were approved in ignorance of Meyer's misstatements and the transferring members transferred from the Fund to the 'daughter' funds without knowledge of the Fund's substantial surplus.

In contrast to the funding level after the transfers, which was 606%, the funding levels of the three daughter funds were 123%, 121% and 116% respectively. The 'unbundling' left the Fund with a very large surplus (which by now must be over R100m), no active members and only fourteen pensioners.

When the board of the Fund applied to the Registrar for the liquidation of the Fund, it was approved. The board thereafter submitted a draft amendment to the rules of the Fund which would permit the payment of the surplus to Pepkor Limited. The consideration of this amendment led the chief actuary of the FSB to discover the initial misstatements by Meyer and the unauthorised transfer of the R9,2m to the executive's fund.

The FSB and the Registrar brought the proceedings in the Cape High Court for the reviewing and setting aside of the approvals and the transfers, and to direct the executive's fund to repay the R9,2m together with interest to the Fund's liquidator.

Acting Judge Owen Rogers granted the relief, but suspended the declarations of invalidity for a period of six months, with the proviso that any party to the action could, on notice to the other parties, apply for the suspension to be lifted, reduced or extended. Pepkor Limited and the executives' fund appealed to the SCA challenging the right of the FSB and the Registrar to bring the proceedings.

In 1977, in a different matter, the appellate division held that if an administrative act had been performed irregularly – be it as a result of an administrative error, fraud or other

circumstance – then, depending upon the legislation involved and the nature and functions of the public body, that body was not only entitled, but also bound to raise the matter in a court of law, if prejudiced.

The appellants contended that, in contrast to certain other sections of the Act, section 14(1) did not specifically give the Registrar the right to apply to court to have a certificate wrongly granted by him, set aside; and that the Registrar accordingly did not have that power. It was further submitted that the appeal procedure provided for in the Financial Services Board Act, 1990 points to the same conclusion.

These arguments were rejected by the SCA as being without merit. Section 14 deals with an important aspect of the regulation of pension fund organisations. It governs the amalgamation of any business carried on by a registered fund with any business carried on by any other person; and the transfer of any business from a registered fund to any person, or from any person to a registered fund.

The section provides that no such amalgamation or transfer 'shall be of any force or effect' unless the prescribed requirements are met. Subsection (2) correspondingly provides *inter alia* that the relevant assets of the bodies amalgamated or the relevant assets of the body transferring its assets shall vest in the body to which they are transferred, 'whenever a scheme for any transaction referred to in subsection (1) has come into force in accordance with the provisions of this section'.

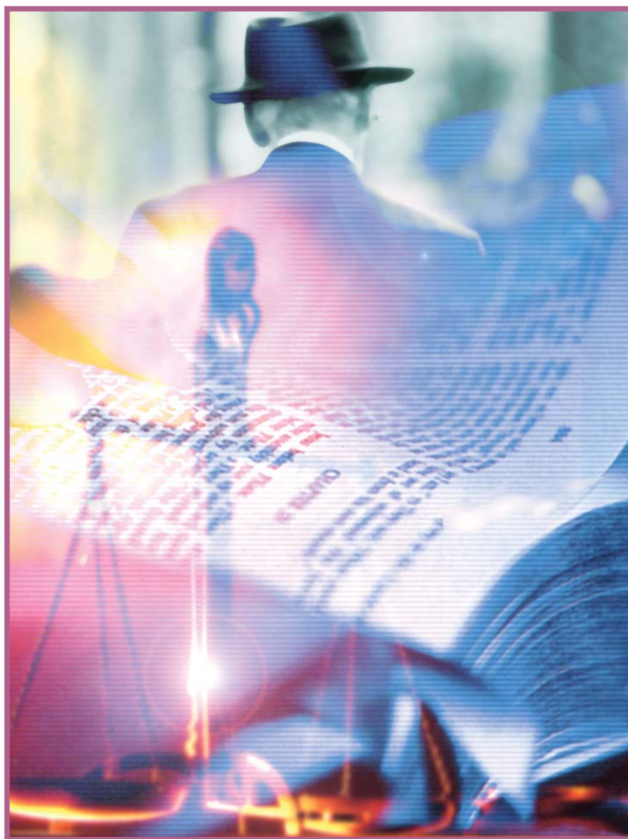
One of these requirements is that the Registrar must be satisfied that the scheme for the proposed transaction is reasonable and equitable, also regarding the other matters specified in subsection (1)(c). The SCA stated that it was unthinkable that if the Registrar were to realise *ex post facto* that there had not been compliance with the section, he could not apply to court to have the transfer set aside. It would indeed be the Registrar's duty to make such an application, if prejudiced.

The appellants claimed that the Registrar had not been prejudiced and that it should be left to those prejudicially affected by his decisions, such as the members of the daughter funds, to take the transfers on review. The SCA found that submission equally without merit.

The Registrar's claim for repayment of the R9,2m was brought by way of an amendment granted subsequent to the insertion of section 6A in 1997 into the Financial Institutions (Investment of Funds) Act, 1984.

The R9,2m was paid by the Fund to the first appellant without following the procedure prescribed by section 14(1). This was not only a contravention of that section, but also contravened section 5(2) of the Act which requires *inter alia* that 'all monies … belonging to a pension fund shall be kept by that fund'.

In terms of section 14(2), it is only when 'a scheme for any transaction referred to in subsection (1) has come into force in accordance with the provisions of this section' that 'the relevant assets … of the body transferring its assets … or any portion thereof shall … vest in … the body to which they are to be transferred'.



The Fund was not intent on reclaiming the R9,2m and the executives' fund was intent on retaining it. The contravention by the Fund of section 5(2) of the Act and the contravention by the executives' fund of section 14(2) of the Act are continuing and the Registrar accordingly has *locus standi* in terms of section 6A to compel the Fund and the executives' fund to cease the contraventions.

The court decided that the FSB had the necessary *locus standi* to approach the court to review the decisions by the Registrar to grant the Section 14 certificates and to set those certificates and the transfers consequent upon them, aside; but that the FSB had no *locus standi* itself to seek an order that the R9,2m be repaid. That power vested only in the Registrar.

The section 14(1) transfers

In relation to the section 14 transfers, the court said that had fraud been proved, that would have sufficed for the relief sought by the FSB and the Registrar because the certificates would have been void. But fraud was not alleged and the review could only have succeeded on some other ground.

On the facts, it was submitted on behalf of the appellants that even had the correct information about the funding levels before and after the transfer been furnished to the Registrar, the Registrar's decision would have been no different.

The SCA, concluded that: 'If the misrepresentations had not been made the initial transfers would not as a fact have been approved as they were. I have carefully considered the detailed argument to the contrary submitted on behalf of the appellants but I am unable to fault the learned trial judge's conclusion. It appears to me to have been entirely justified.'

The appellants submitted that the size of the surplus remaining in a defined benefit fund is legally irrelevant to the exercise by the Registrar of his powers under section 14(1). The submission was that because the Fund and the 'daughter' funds were defined benefit funds and not defined contribution funds, transferring members can have an interest only in the security of the benefits to which they will become entitled; and once they are adequately secured, as they were in this case, any surplus remaining in the fund was effectively none of their business: the employer could use the surplus for a 'contribution holiday' but the members were not entitled to it.

But section 14 required at the time when the transfer applications were approved, and still requires, that the Registrar 'be satisfied' *inter alia* that the scheme for the proposed transaction is

To p.19

Fedsure Life fact-finding finalised

The inspection report relating to Fedsure Life, the long-term insurer that was taken over by the Investec Group, has been released after the high court granted the FSB permission to make it public.

At the root of the inspection were the interests of Fedsure Life's policyholders. The inspection was a fact-finding mission aimed at uncovering the truth of what happened at Fedsure Life, specifically with regard to corporate governance and policyholders' expectations.

What also prompted the inspection was the need for an objective consideration of the appropriateness of the legislation and the effectiveness of the supervisory practices of the FSB.

The investigation covered the affairs of Fedsure Life over four years. The FSB was convinced that the public interest required the truth to be exposed as many of the affected policyholders and pension fund members were ordinary people who could not understand what went wrong with their life savings.

The inspection was not ordered because Fedsure Life was found to be failing in the prescribed capital asset requirements or solvency margins; or that any irregularities such as statutory contraventions, dishonesty or improper actions had been brought to the FSB's attention. Fedsure Life was also not in danger of being unable to meet its contractual commitments, or other regulatory matters which normally induce an inspection.

Public concerns were aggravated by media reports on the forfeited bonus and the takeover negotiations between the Fedsure Group and the Investec Group which involved Fedsure Life.

Reasons for publication

The report sends a strong message to the insurance industry that their conduct is susceptible to disclosure through an inspection.

The report could be seen as a treatise on long-term insurance business for all those not knowledgeable in the field. Non-executive directors of life insurers are now likely to appreciate that their role is not limited to the introduction of external expertise in the company. The same applies to professionals like actuaries and auditors who play a vital role in the regulatory and supervisory framework. They must appreciate that, like the regulator, they may be held accountable publicly.

It is the FSB's opinion that the report will set new standards for the life industry which will have positive effects on the level of responsibility of all those associated with the industry, including the regulator.

Since the promulgation of the Long-term Insurance Act, 1998 and the Inspection Act, 1998, the tide has turned in favour of openness, full disclosure, accountability, access to information and the consumer rights.

Findings

The report contains no findings of statutory contraventions, criminality, dishonesty, fraud or bad faith. It is published to inform the industry and consumer that despite good intentions, things can go wrong, and should therefore be actively watched and properly managed.

The FSB will therefore not refer the report to the prosecuting authorities. However, the legislative proposals in the report have been receiving attention for some time.

Procedure

The investigation and the record of findings took eleven months, from mid May 2002 to end April 2003, before the final report was handed to the FSB. The FSB made copies available for comment to a number of interested parties, when the first edition of the report became available in December 2003.

The inspectors, after considering comments received, delivered their final report on 23 April 2003. Copies were once again given to all those parties who had previously commented.

Value of report

The publication of the report presents a lesson to the consumer on various aspects: the intricacies, advantages and risks associated with long-term investments; that unpredictable external factors such as the capital markets may influence the investment; that would-be policyholders should ask questions on matters such as the track record of the company and the proficiency of its management; and that policyholders should keep on enquiring about the activities of their insurer in respect of take-overs, mergers, financial results, major changes in management or shareholders.

The report can be seen as a treatise on what long-term insurance business is or should be about. Parties which participate in this business, as policyholders or members of pension funds, will all benefit from reading the report.

The report sets out the historical events and factual findings from 1998 to the date the investigation started. This is followed by an analysis of the FSB's actions, the inspectors' views on the professional conduct of Fedsure's directors and management, as well as questions and answers on whether policyholders' reasonable expectations have been met.

The inspectors dealt with matters such as directors' fiduciary duties, as well as the care and diligence imposed by law. The report also contains the inspectors' recommendations to the industry and other role players, such as actuaries, auditors, ombudsmen and the regulator.

André Swanepoel, FSB's deputy executive officer: Insurance and Jeff van Rooyen, FSB's executive officer, addressed the media on the Fedsure report.

Way forward

The inspectors made several recommendations to which the FSB is giving urgent attention. These include:

* The demarcation of shareholders' and policyholders' assets and enforcement of asset liability management principles and procedures.
* The revisiting of the regulations pertaining to investments from a solvency point of view as well as the spreading of assets, distinguishing between those assets covering the liabilities and the free assets.
* The imposition of a compulsory annual analysis of surplus in a more detailed form than the current basis.
* A re-evaluation of corporate governance requirements, the role of the independent non-executive director, the terms of reference of board committees, communications between the board and management and the statutory enforcement of selected elements thereof in a transparent environment.
* An evaluation of the marketing, disclosure, product design, pricing and investment mandates of the family of smoothed bonus policies.
* An assessment of the independence and statutory powers and responsibilities of specifically the statutory actuary and the approved auditor(s) of the company.
* More effective measures to protect the interests of policyholders in the event of take-overs and mergers;
* The establishment of an integrated ombud system to deal with consumer complaints against financial institutions.

The report is available on the FSB's website at *www.fsb.co.za*

Source:
FSB Media Release, 13 June 2003

Industry and institutions should act in best interest of pension fund members

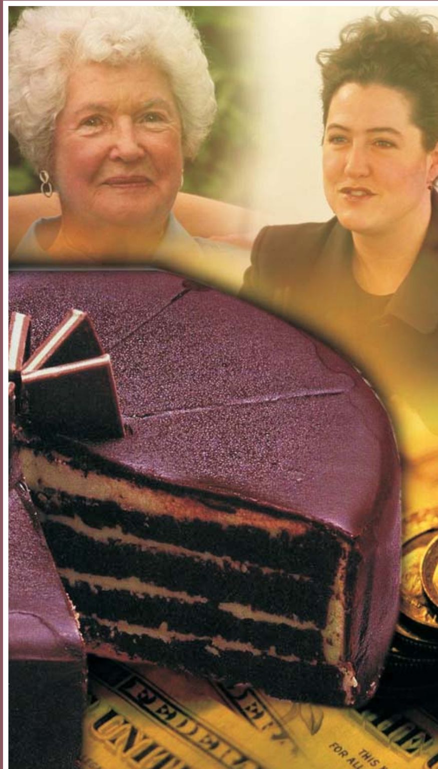
The Pension Funds Second Amendment Act, 2001, requires that every retirement fund with actuarial surplus, or an excess of assets over liabilities, apportion the surplus between stakeholders.

The board of the fund must apportion surplus funds at the first actuarial valuation after 7 December 2001, the date on which the Act became law, or earlier if the fund was converted from a defined benefit to a defined contribution, or if the fund was liquidated. This means that all the apportionments should have a base date before 7 December 2004.

Apportionment schemes should be submitted to the FSB within 18 months of their effective date. But because of delays in the publication of the regulations detailing the methods and assumptions to be used, some funds have been granted extensions. Payment to members will only take place after the FSB has approved the scheme.

The process to establish surplus apportionment starts with a valuation of the fund to determine the actuarial surplus, after setting aside such contingency reserves as the board deems appropriate. Contingency reserves must make provision for matters such as the anticipated cost of the surplus apportionment exercise. To this surplus must be added "surplus utilised improperly". This will require the board to investigate the financial history of the fund. If there is surplus after the valuation, the boards must apportion it.

Former members and pensioners get the first slice of any actuarial surplus as their



benefits must be increased to minimum levels. Thereafter any residual surplus is split equitably between stakeholders, i.e. former members, pensioners, current members and the employer.

The board has to appoint a person to represent the interests of former members, and must obtain records for all former members. The role of the representative is to scrutinise the process, facilitate communication with former members and ensure that former members get a fair deal. Former members who anticipate that they might get something in the surplus apportionment are encouraged to send their contact details to their former funds at the office of administrators.

Industry experts and institutions who aired their criticism of the pension fund surplus apportionment regulations, are not acting in the best interest of pension fund members.

"The regulations and board notices that followed the promulgation of the Act were the outcome of a long consultation process between the retirement industry, organised labour, Business South Africa and the FSB," said Dube Tshidi, the FSB's deputy executive officer: Retirement Funds and Friendly Socieities. "Throughout the consultation period everybody had the opportunity to make comments or contributions.

"There is no such thing as a perfect law. But we do expect people to look at and apply the surplus fund legislation to help pension fund members get their portion of the surplus, and not to find ways and means to prevent people from getting their fair share.

"In light of this, future amendments cannot be ruled out. It should however not be used as an excuse not to implement the legislation as it stands now and thus deny members the opportunity to share in the surplus."

The FSB has initiated the setting up of a database and call centre to enable former members to call the FSB, toll-free, and find out the contact details of their former funds. The FSB's toll-free numbers are **0800 110443** and **0800 202087**. Once the database and call centre are set up, the FSB will run a communication campaign nationally to tell people about the facility.

Call centre experiences influx of calls

The FSB's call centre has experienced a substantial increase in the number of calls since its inception in August last year.

Selvan Govender, FSB's call centre manager, says the call centre expects a further influx due to pension fund surplus queries and enquiries regarding the registration of financial advisers and intermediaries.

"We have focused on training and skills development to deal with the expected flood of calls," adds Govender. Three of the four call centre operators have attained National Qualification Framework Level 2 certificates for superior telephone skills. The call centre now also has a walk-in reception, where call centre personnel will assist customers in person.

The centre has purchased software, which not only enables the recording of all calls, but is also able to capture individual statistics for each operator, as well as monitoring trends. "The FSB prides itself that it will be the first call centre to install the Heat Plus Call Centre software," says Govender.

"After the FSB's deputy executive officer: Retirement Funds and Friendly Societies discussed surplus and unclaimed benefits on SABC3, the call centre received more than two thousand calls the following day," says Selvan Govender, call centre manager. Left of him is call centre operator, Caroline Hlongwane.

What does the revised Financial Services Ombudschemes Bill entail?

By Louis Wessels, FSB Legal Department

The revised Financial Services Ombudschemes (FSOS) Bill was released recently for comment by interested parties.

The amendments proposed to the Bill, as gazetted on 19 March 2002, are not radical. The two main features of the Bill remain as before: The recognition of voluntary ombud-arrangements subject to the schemes complying with certain minimum criteria prescribed in the Bill; and the creation of a statutory ombud to deal with complaints that could not be dealt with by any of the voluntary schemes.

Apart from having to qualify and maintain the standards set by the Bill, industry schemes will be free to determine their own terms of reference. Each scheme will decide its own constitutional structure, appoint its ombud, set the jurisdiction of the ombud regarding type of complaint and limit on amounts, what class of client will qualify for the submission of complaints, the location of office, staff complement, funding arrangements, etc.

Briefly, the Bill preserves the independence of recognised schemes to look after their own affairs. However, ombudschemes are likely to go about this exercise very carefully as complaints against participating members not dealt with by the scheme, may land up in the jurisdiction of the statutory ombud.

The introductions to the Bill, compared to the gazetted version, are essentially the following:

* the extension of the activities of the governing Financial Services Ombudschemes Council to facilitate the lodging and distribution of consumer complaints;
* a provision making it clear that the ombuds of voluntary schemes may not deal with complaints where the Ombud for Financial Services Providers (FAIS Ombud) may exercise jurisdiction;
* grace being allowed to existing schemes to continue operations for twelve months after the promulgation of the Bill into law;
* debarring the operation of any dispute resolution scheme other than one recognised under the Act, by any financial institution supervised by the FSB.

Extended powers of Council

With its increasing efforts to give effect to its mission to promote programmes and initiatives to inform and educate consumers in the financial services industry, the FSB has become more aware of the need to assist consumers in finding their way to the correct complaint resolution mechanism. The FSB's own call centre has been in operation only since 1 August 2002. It has been attracting increasing enquiries from consumers regarding various aspects of the FSB and industry, with complaints and where they should be submitted, forming a central theme. The proliferation of ombudschemes in the country has contributed to the confusion.

Hence, the provision that the Council's objective, through a process of co-ordination of scheme activities and assistance to consumers, is to provide a comprehensive and integrated complaint management and dispute resolution system for consumers in the financial services industry. To this end the Council is empowered to oversee the establishment and operation of an electronic communication system, such as a website, and call centre (probably availing itself of the infrastructure of the FSB's call centre) to refer consumers to the right ombud; to maintain contact with consumers and to promote their education regarding resolution forums; to develop and promote best practices for complaint handling; and to ensure periodic independent review and reporting on the conformance by ombudschemes with standards prescribed by the Council and the FSB.

While the revised Bill represents a truly South African model, similar developments in other jurisdictions did not escape the notice of the drafters of the new provisions. Last year the three independent industry schemes in Australia decided to co-locate into one building and to provide a central port of entry for all consumer complaints. The three ombuds participate jointly in public relations and educational programmes. More and more services are being shared. In Canada a financial services ombuds network was established late in 2002, with similar objectives. It operates a centre to provide financial services to consumers with single-window access to high-quality, independent, impartial and effective complaint resolution services.

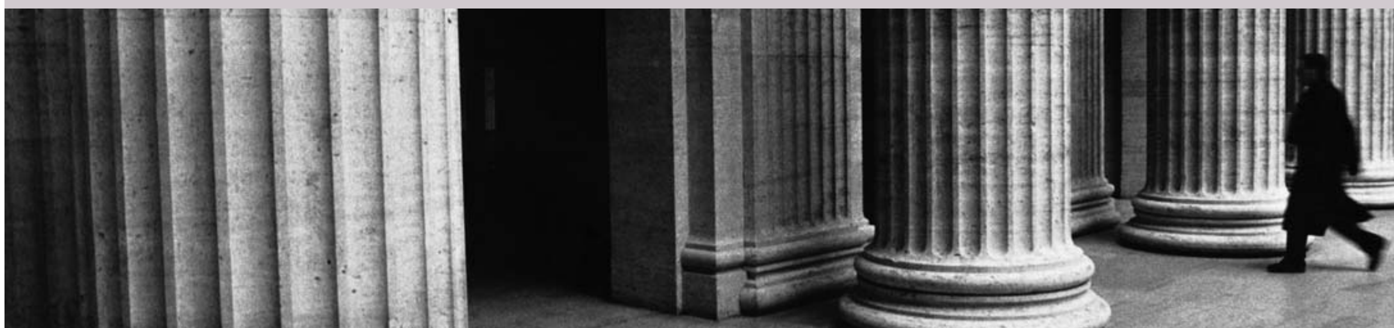
Jurisdiction of FAIS Ombud

All ombudschemes – voluntary and statutory – operate in a specialised area. In line with the functional approach of the Financial Advisory and Intermediary Services (FAIS) Act, 2002, the legislature established a dedicated office to deal with complaints arising from the application of the Act. For the sake of consistency, to avoid forum arbitrage, and to enable the FAIS Ombud to develop expertise in this field, FAIS complaints must be dealt with by the FAIS Ombud. FAIS and FSOS have taken care of the situation where uncertainties and overlaps in jurisdiction may occur.

Establishment of new schemes

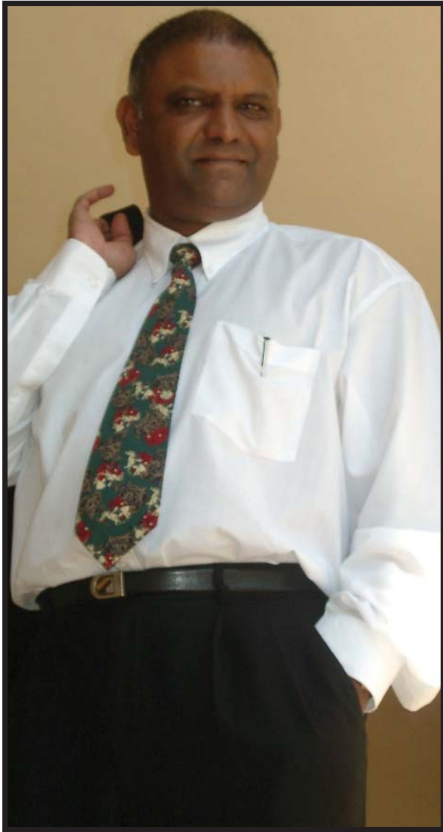
Bearing in mind that the Bill aims at standard setting, it was simply correct to provide that if ombudschemes are to be operated at all, they must seek recognition under the Bill. This applies to all financial institutions supervised by the FSB. However, the Bill provides for exemptions in appropriate circumstances.

On the assumption that the Bill in its revised form will be adopted by Parliament, the new law is expected to become effective early next year.



FSB appoints first FAIS Ombud

By Astrid de Vos, communication and liaison assistant, FSB



Pretoria attorney, Charles Pillai, will become the first Ombud for Financial Services Providers in terms of the Financial Advisory and Intermediary Services (FAIS) Act, 2002.

The appointment of Pillai, director of the Pretoria office of the Legal Resources Centre (LRC), is a further important step in implementing the FAIS Act.

The Office of the FAIS Ombud, the fifth Ombudsoffice in the financial services sector in South Africa, provides a dispute resolution mechanism for client complaints in the financial services industry.

Other dispute resolution offices include the Pension Funds Adjudicator, a statutory office, and the ombuds for the long-term and short-term insurance industries, as well as the Banking Adjudicator, which are non-statutory offices.

Pillai's first priority will be staffing the Pretoria office and getting it into operation when it officially opens in September.

"It is a matter of rolling up one's sleeves and getting down to business," he says.

Uppermost on the agenda for the new Ombud is a national consumer education drive to create awareness of the rights and responsibilities of financial services consumers.

"It is important that people understand the function of the FAIS Ombud. It is not a consumer watchdog, but a mediator and arbitrator that works with industry and consumers to ensure integrity and justice, while maintaining its independence," Pillai adds.

Pillai started his career as a lawyer in Chatsworth, south of Durban, in the early eighties. He had a general law practice, and his experience includes litigation, conveyancing and commercial law.

"I have always had a quest to serve the community, and taking this position underpins everything I have done thus far in my career as lawyer and in my involvement in the community," he says.

Pillai finds mediation rewarding. "It is about building bridges and relationships," he says.

He displayed an interest in mediation and conflict resolution early in his career with *pro bono* work for victims of racism, among others. It culminated in his involvement with the drafting of the United Nations NGO declaration on racism at the World Conference Against Racism held in Durban in 2001.

Pillai attained a Bachelor of Arts degree at the University of Durban-Westville in 1975. He followed it up with a BProc degree from the University of South Africa in 1979 while he completed his clerkship. In 2001 he received an LLB from the University of Natal and Unisa. He is enrolled for an LLM in Administrative and Constitutional Law at the University of Pretoria.

He joined the LRC, a public interest law firm, on 1 December 1998. He was appointed director of the Pretoria office in April 1999. The LRC is involved in litigation and advocacy in areas such as children's rights, land restitution, education, governance and administrative justice, among others.

Apart from his professional commitments as a lawyer, Pillai pursues an interesting hobby as an actor and a playwright, something that he has had to put on hold since his involvement in public interest law.

FSB approves first recognised bodies for FAIS registration

In June, the FSB approved the authorisation of the first two recognised bodies that applied to assist with the registration of financial advisers and intermediaries.

The two bodies are the Insurance Brokers Council (IBC) and the Group Administrators Forum (GAF). The latter is a newly formed body representing funeral business administrators.

Manasse Malimabe, the FSB's head of the Financial Advisory and

Intermediary Services (FAIS) Department, says this puts into motion the massive licensing process required in terms of the Financial Advisory and Intermediary Services (FAIS) Act, 2002.

An estimated 20 000 entities will apply to the FSB for licences. The FSB will be delegating this function to recognised bodies that meet certain criteria in order to speed up the process and cut costs. Functions delegated to these bodies include the processing of licence applications and registration of compliance officers.

The FSB is considering the approval of another ten industry bodies.

Source:
FSB Media Release, 12 June 2003

FSB boasts increase in staff numbers and achieves employment equity targets

"We have achieved a dramatic increase in staff numbers of close on 54 percent over the past three years, while managing to reduce staff turnover to way below that of the industry and reaching our employment equity goals. This has been achieved while maintaining the cost of regulation within reasonable levels," - Jeff van Rooyen, FSB executive officer.

Three years ago, a Financial Sector Assessment Programme (FSAP) conducted by the World Bank and the International Monetary Fund (IMF) established that the FSB was under-resourced.

"Since then, our responsibilities have grown considerably to include facilitating consumer education, running a call centre and supervising financial advisers and intermediary services," Van Rooyen says.

"In response to the FSAP Report and to provide for the increased scope of work, we have increased our staff complement considerably. Our total staff, including contract and bursary staff, was 226 on 31 March 2003, an increase of close on 54% over the 2000 figure of 148," he explains.

The staff complement (including contract and bursary staff) as at 31 March 2003 was as shown in table one.

Van Rooyen says the management of diversity and the achievement of employment equity goals remain priorities, adding: "We have managed to make great strides towards the achievement of our overall target during the past financial year and appointed a significant number of senior personnel in terms of our equity policy.

"The FSB had 56% female staff and 59% black staff on 31 March 2003 and the top management profile was 32% black."

Despite the dramatic increase in staff numbers, Van Rooyen says the FSB has managed to reduce staff turnover to around 5,3%, a figure which is less than half of the industry rate.

He ascribes the low turnover rate to the FSB's progressive human resources policies which embrace sound staff training and development policies. Table two compares the staff turnover rate from March 2000 to March 2003.

Table one

Staff complement as at 31 March 2003:

	2003	%	2002	%	2001	%	2000	%
Black females	69	31	55	27	36	23	31	21
White females	56	25	53	26	44	27	41	28
Black males	64	28	59	29	42	26	36	24
White males	37	16	38	18	39	24	40	27
TOTAL STAFF	**226**	**100**	**205**	**100**	**161**	**100**	**148**	**100**

Table two

Staff turnover rate from March 2000 to March 2003:

Year	Annual staff turnover rate
2000	11.59 %
2001	6.46 %
2002	5.14 %
2003	5.29 %

FSB's Information Technology to ensure compliance with Electronic Communications and Transactions Act

By Hennie Viljoen, systems development manager, Information Technology, FSB

The FSB is conducting a legislative review to identify inconsistencies between legislation or regulation, and the Electronic Communications and Transactions Act, 2002 (ECTA).

One objective of this review is to specify the operational and technical standards of IT systems, processes and procedures, to comply with the requirements of the ECTA. The FSB is giving special attention to the operational and technical standards contemplated in section 28 of the ECTA in terms of financial services legislation that are mentioned in section 27 of the ECTA.

This includes the format in which data messages and documents must be filed, created, retained or issued; the format and manner of association of electronic signatures with data messages; the criteria that must be met by authentication service providers; and appropriate control processes and procedures to ensure integrity, security and confidentiality of data messages or payments.

The FSB will apply these standards to document management, the issuing of licences or approval, the manner of payment for services rendered, and e-mail.

The area of document management has been identified as a major area of deployment of e-business technology to support and streamline the regulatory function of the FSB. For this reason, the FSB has identified a number of standards to ensure compliance with the ECTA. It should be possible, for instance, to identify the identity and authority of the sender of documents accepted in electronic format. Mechanisms should be in place to ensure that documents arrive intact at their destination, that they are tamper-free, and that they are stored in a manner that enables easy retrieval according to subject or category. The successful recovery in case of technical or physical disasters should also be guaranteed.

These requirements can be met by interactive web applications that will function as remote front-ends for uploading of documents, and back-end applications that will allow processing of uploaded documents. Authentication can be managed by registration of authorised users with encrypted passwords, and access rights defining the functions that each user is allowed to perform.

Documents should be indexed before uploading, according to pre-defined index criteria that will enable easy retrieval by back-end applications. Electronic signatures will be considered legally binding if they appear on documents which cannot be edited, or when they are digitally attached to documents and authenticated by a trusted service provider.

The FSB has one operational e-business system that meets all these requirements. Pension fund administrators have authorised users registered with the FSB, who are allowed to create work directly in the Pensions Department's workflow system. This is performed through a web front-end system by uploading and indexing the electronically signed documents according to predefined index criteria. The Pensions Department then processes these workflow cases which normally conclude in the issuing of licences or some kind of approval or rejection.

Payment is verified by the back-end workflow system by managing invoice or deposit accounts that each administrator has with the FSB. The FSB will implement a similar system for the Financial Advisory and Intermediary Services Department.

The FSB has a formal Disaster Recovery Plan (DRP) in place that consists of real-time data mirroring, daily backups, and a contractual partnership with a DRP service provider in case of a physical disaster.

The IT Department is also developing a system that will allow pension fund administrators to submit auditors' digitally approved financial statements electronically, which will then be imported into and validated by the FSB's workflow system. This system will eliminate the need for producing and signing of hardcopies, or manual capturing of financial statements both at source and at the FSB.

The FSB realises that e-mail is now legally binding as long as it can be proved that it is the original and has not been altered. Signatures on e-mail are now permissible as evidence. As a result, the FSB can be held liable for messages sent out by employees. For this reason it is a priority for the FSB to educate all e-mail users about the responsibility.

The FSB is also looking at deployment of e-mail archiving tools that will facilitate automatic and manual saving and retrieving of e-mail messages according to predefined rules.

Can insurers hold shares in their holding companies?

There appears to be some uncertainty about the legal position of long-term insurers holding shares in their holding companies. The basic position is explained in this overview by Gillie Gehle, chief law adviser, Sanlam Life.

In this overview section 19A refers to that section of the Insurance Act, 1943 (the 1943 Act), sections 32(2) and 34 refer to those sections of the Long-term Insurance Act, 1998 (the 1998 Act), and sections 39 and 85 to 89 refer to those sections of the Companies Act, 1973. "Registrar" means the Registrar of Long-term Insurance, and "insurer" means a long-term insurer as defined in the 1998 Act.

Insurers have a unique financial make-up. Unlike other companies, they have a shareholder fund and policyholder funds. The insurer, in reality, holds the assets in a policyholder fund as trustee for the benefit of the policyholders concerned. But, in law and form, the insurer does not hold these assets as trustee.

The legal position of long-term insurers holding shares in their holding companies is regulated by legislation, and has changed considerably over the last few years.

Position before section 19A was inserted in the 1943 Act

There was a time when insurers were not permitted to hold shares in their holding companies. Section 39(1) prohibited it. There were, however, two exceptions.

First exception

Section 39(1), as confirmed by section 39(2), did not apply to the holding by a subsidiary of shares in its holding company as trustee - namely where the subsidiary held the shares not for its own beneficial ownership, but for the beneficial ownership of another. Section 39(1) applied only to the holding by a subsidiary of shares in its holding company for its own beneficial ownership.

This makes legal and commercial sense. For example, a listed company has a subsidiary, which is a professional trust company. The subsidiary is appointed as the trustee of a trust. As the trustee, it holds the trust assets, which include shares in the listed company. It does not hold the trust assets for its own beneficial ownership, but for the beneficial ownership of the trust beneficiaries. It simply would not have made legal and commercial sense if the subsidiary would have been prevented by section 39(1) from holding those shares as part of the trust assets.

As trustee, a subsidiary could hold up to 100% of the shares in its holding company, and could exercise the voting rights of those shares. It seems unlikely that an insurer would have held shares in its holding company as trustee.

Second exception

Section 39(1) also did not apply to shares a subsidiary acquired in its holding company before it became a subsidiary of its holding company. Section 39(3)(a) contained this exception. A subsidiary could so hold up to 100% of the shares in its holding company. But, it could not exercise the voting rights of those shares.

Position after section 19A was inserted in the 1943 Act

Section 19A was inserted in the 1943 Act specifically to allow insurers, with the prior approval of the Registrar, to hold, in their policyholder funds, shares in their holding companies. The shares were, in terms of section 19A(1)(a), deemed to be held as trustee. Therefore, by virtue of section 39(2), the prohibition of section 39(1) did not apply to these shares. Restrictions that applied to this shareholding included not being able to hold more than 10% of the shares in the holding company, a limit imposed by the Registrar, and not being able to exercise voting rights.

Position after section 19A was replaced by section 32(2)

Except for minor contextual changes, section 32(2) is a repeat of section 19A(1). The position under section 19A(1) simply continued without change under section 32(2).

Position after the Companies Act was amended in 1999 to allow subsidiaries to hold shares in their holding companies

This amendment of the Companies Act (the 1999 amendment), which is reflected mainly in the amended section 39(1) and the new sections 85 to 89, allowed subsidiaries to acquire shares in their

holding companies, with the restriction that all the subsidiaries of a holding company together may not acquire more than 10% of the issued shares in the holding company.

The 1999 amendment imposed, in sections 85 to 88, certain requirements regarding the buy-back of shares, which apply also to the acquisition of shares by subsidiaries in their holding companies, such as:

* The subsidiary must be authorised by its articles of association to acquire shares in its holding company.
* The acquisition must be approved by a special resolution.
* The subsidiary must comply with liquidity and solvency tests before making the acquisition.

While a subsidiary may hold shares in its holding company that it "acquired in accordance with section 89", the voting rights of those shares may not be exercised by the subsidiary, and the percentage of votes able to be cast at a meeting of shareholders must be reduced by the number of shares held by the subsidiary.

Summary of the position under section 32(2) after the 1999 amendment

Shares an insurer may hold in its holding company - in its shareholder fund	**Shares an insurer may hold in its holding company - in its policyholder funds**
General position - sections 89 and 39(1) * up to 10% * no voting rights	General position - shares deemed to be held as trustee - section 32(2) * up to 100% - but limited by the Registrar, for an insurer who applied for approval after the 1999 amendment, to so many as will, together with the shares in its holding company held by the insurer in its shareholder fund, and together with the shares in its holding company held by other subsidiaries, be not more than 10% of the issued shares in its holding company * no voting rights
Shares acquired before the insurer became a subsidiary of its holding company Position now uncertain	Shares acquired before the insurer became a subsidiary of its holding company As under general position above - section 32(2)

Position under section 32(2) after the 1999 amendment

The 1999 amendment has not altered the position under section 39(2), nor, in particular, the position under section 32(2) read with section 39(2).

Apart from shares in its holding company that an insurer holds in its policyholder funds under section 32(2), it may also, under section 89, acquire and hold, in its shareholder fund, not more than 10% of the shares in its holding company. (See table above)

It makes sense

It makes commercial and regulatory sense that an insurer is able to hold shares in its holding company in both its shareholder fund under section 89, and its policyholder funds under section 32(2).

Take, for example, the following situation: A holding company has several subsidiaries, one of which is an insurer. One of the other subsidiaries already holds 10% of the shares in the holding company, which it acquired under section 89.

A pension fund now takes out a policy with the insurer. It pays the premium under the policy in kind, namely by transferring assets to the insurer. These assets (the premium under the policy) include shares in the holding company. If the effect of the 1999 amendment were that an insurer may now acquire shares in its holding company only under section 89, the insurer would not be able to accept these shares as part of the premium. The pension fund would then have to sell these shares in order to pay the sale proceeds as a premium in cash to the insurer. Such a forced sale could be to the detriment of the pension fund and its members.

This is where section 32(2) comes to the rescue. It permits the insurer to acquire and hold these shares, in the policyholder fund concerned, with the prior approval of the Registrar, and subject to any conditions the Registrar may impose. The Registrar may, for example, then impose a condition that these shares be reduced in a responsible and beneficial manner over a specified period.

To acquire shares under section 89, the subsidiary must comply with the requirements in sections 85 to 88, to the extent that they apply. This entails, among others, that the acquisition must be approved by a special resolution of the shareholders of the subsidiary.

It is impractical, and could not have been the intention of the lawmaker, that an insurer must comply with these requirements every time it has to accept shares in its holding company as part of a premium under a policy.

Fortunately section 32(2) provides for this situation, proving that it has not only commercial merit, but indeed is an indispensable regulatory tool.

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Insider trading settlements have more pros than cons

By Gerhard van Deventer, executive director: Insider Trading Directorate, FSB

The Insider Trading Act, 1998, came into operation on 17 January 1999. The most important feature of this legislation was that it created a statutory civil action (not unlike a class action), on behalf of persons who could have been prejudiced by unlawful transactions. The plaintiff in such an action is the FSB. However, aggrieved parties are not deprived of their common law remedies.

FSB/Ingledew case

On 2 July 1999, Skills Accel Limited (Skills), a public company listed on the JSE Securities Exchange South Africa, announced through the Stock Exchange News Service that it had made certain operational acquisitions and had appointed certain additional directors. On the same day, the share price of the company increased significantly.

Two directors of Skills purchased shares in the company before the announcement, which resulted in the Insider Trading Directorate (Directorate) taking legal action against them. On 26 May 2000, summons was issued against the directors as first and second defendants. The first defendant filed his plea shortly afterwards, but the second defendant (the defendant) claimed that he was unable to plead without first having access to all the information and documentation in the FSB's possession. The FSB was not prepared to grant the defendant this access, which led to a High Court application.

High Court Application

The application was firstly based on a request in terms of rule 35(14) of the Rules of Court which stipulates that a defendant may obtain documentation for purposes of pleading.

The court came to the conclusion that the defendant did not make out a case that he needed the documents for purposes of pleading.

When the FSB enforces its anti-insider trading legislation through the civil courts, the rules of civil procedure are adequate to ensure a fair and equitable trial for the defendant. This was underlined by the rejection of the arguments on behalf of the defendant that he should have all the rights of an accused person in a criminal matter, merely because insider trading is also a criminal offence. The Court commented that … *"civil proceedings have their own rules relating to access to documents, rules that were fair and even-handed long before it was necessary to extend an accused's right to access to the Police docket."*

The second leg of the application was based on the request for information in terms of section 32 of the Constitution which gives everyone a right of access to information held by the state or another person, required for the exercise or protection of rights.

In terms of section 32 an individual's right of access to documentation is extensive. However, in terms of section 36 of the Constitution, such a right may be limited by a law of general application. This means another law, which is applicable to everybody, and that is reasonable and justifiable in an open and democratic society, may limit the individual's right to obtain documentation. The court found that Rule 35(14) referred to above is such a law.

This conclusion brought the issue back to the point that the defendant could only obtain documentation in terms of Rule 35(14) to the extent necessary for purposes of pleading.

Application for Leave to Appeal in the High Court

The defendant was however not satisfied with the judgment and applied to the High Court for Leave to Appeal to the Constitutional Court. The High Court was of the view that there was no reasonable prospect that another court would come to a different conclusion and the application was dismissed.

Application for Leave to Appeal in the Constitutional Court

The defendant decided to take the matter further and applied directly to the Constitutional Court for leave to appeal. In the ensuing proceedings the defendant raised the same constitutional issues.

Firstly, he argued that he was entitled to the information under Rule 35(14) by pointing to the penal nature of the action against him. (The civil action in the Insider Trading Act is based on the profit made or the loss avoided by the offending individual, as well as a penalty of three times such amount.) The Constitutional Court said that only relevant information required for purposes of pleading may be acquired under Rule 35(14). The court found that *"... There is no reasonable Constitutional construction of the rule that could broaden such purpose to accommodate the construction of it contended for by the defendant."*

Secondly, the defendant also relied on section 32 of the Constitution to gain access to the information. However, he took this step without seeking to have Rule 35(14) declared unconstitutional.

The court found that it was not in the interests of justice to grant leave to appeal. The court held the view that the defendant was not prejudiced by the refusal of the High Court, because he did not need the information to plead. The court also referred to the pre-trial discovery procedures that would assist the defendant to some degree at a later stage. The point was made that the defendant can, through these two mechanisms, obtain

all the information relevant to the issues for purposes of trial. (The application as drafted by the defendant required the FSB to give him all information, whether relevant to the trial or not.)

One of the arguments raised by the defendant was that such documentation might yield further defences that he was not aware of. The court made the important observation that, having regard to the nature of the allegations (insider trading), *"... It is difficult to fathom what other possible defences could emerge from information held by others."* The court came to the conclusion that *"... whether the allegations are true or not, the defendant does not require information about what other interrogatees said in order to determine his defence".*

As a result the application for leave to appeal was dismissed on 13 May 2003. The court ordered the defendant to bear the cost of the application, including the cost attendant upon the employment of two counsel.

Implications of the judgment

The request for information was made before the Promotion of Acces to Information Act, 2002, became law, and therefore has limited application as a legal precedent. However, the judgment is not without value.

Firstly, the court made it clear that the rules of civil procedure provide adequate protection for a defendant in an insider trading case. This means that when the FSB utilises this enforcement option, it is not prejudiced by the additional burden placed on prosecuting authorities in criminal cases.

Secondly, the court was of the view that insider trading is a relatively simple claim that a defendant can plead to without requiring excessive information.

The history of the case to date raises another facet of interest. The Insider Trading Directorate has instituted legal action in 24 cases since its inception in 1999. In 17 of those cases, the Directorate accepted a settlement offer, which obviated the need to go to trial. These settlements were always for three to four times the profit made or loss avoided by the individuals, and their names were published in the media. This has sometimes evoked the criticism that the FSB should not accept settlements, but instead should pursue litigation.

The present case has taken three years to the point where the defendant must file his plea. The phases of the litigation that traditionally extend the duration of court cases, namely waiting for trial dates, postponements and obtaining judgments, have not even been reached yet. Taking into account that all the settled cases have been finalised and in excess of 600 claimants have already received compensation, the decisions of the Directorate to accept settlement offers have proved to be prudent.

Stay away from Gibson, warns FSB

Source: FSB Media Release, 12 May 2002

The FSB issued a warning to consumers to exercise caution in doing business with Robert Gibson.

The FSB's deputy executive officer: Market Conduct and Consumer Education, Gerry Anderson, said the FSB believes that Gibson, who is under FSB investigation, was involved with an approved investment management company, Bridgemoat (Pty) Ltd.

Gibson's involvement with Bridgemoat, situated in Sunninghill, Johannesburg, is also under investigation. Other companies that Gibson may be representing are Future Indefinite Investments (Pty) Ltd and Mortgage Bond Finance and Services (Pty) Ltd. These companies are not approved to conduct investment management business.

The FSB investigation follows complaints from investors who lost money through dealings with Gibson and his companies Future Indefinite Investments and Mortgage Bond Finance and Services. One complaint was from a large bank that reported that Gibson was taking investments and telling clients that the investments were guaranteed by the bank when that was not the case.

The FSB's inspection under section 3 of the Inspection of Financial Institutions Act, 1998, into the affairs of the companies revealed that Gibson took millions from investors under the guise that it will be invested in bonds on the bond market.

Gibson also uses agents to sell financial products. The FSB believes that he is still operating despite the investigation into his companies. The FSB wishes to caution people contemplating any business with him or any of his representatives.

Gibson operates from his home in Queenswood, Pretoria, and also has offices in Johannesburg. He uses agents all over the country, as well as in Namibia, and canvasses money for foreign investments, among other things.

The Special Commercial Crimes Unit of the South African Police Service (SAPS) is investigating complaints of fraud and theft against Gibson. People who have invested money or who have had other dealings with Gibson, are asked to contact the investigating officer, Inspector Johan van Staden, at telephone number 082 800 6722.

Central securities depositories to merge

Following discussions between the shareholders of Share Transactions Totally Electronic, (STRATE), the Central Depository Ltd (CD) and Universal Exchange Corporation Limited (Unexcor) to merge these entities, STRATE made a formal offer in January to acquire the entire business of Unexcor and CD as a going concern. The finalisation of this transaction is dependant on a favourable due diligence investigation by STRATE into Unexcor and CD, along with the FSB's approval and the support of the Competition Commission.

"The merger will have a number of cost and efficiency advantages over time," says Norman Müller, FSB's head: Capital Markets. "These advantages are to be gained through the economies of scale and of scope arguments, which will further improve the competitiveness of the South African financial markets compared to its major foreign counterparts. The merged entity will also facilitate and simplify the introduction of a Central Securities Register, which is being investigated. The merger will simplify the FSB's regulatory duties and responsibilities regarding the regulation of clearing and settlement services in South Africa. It further aims to become the preferred provider of financial market clearing and settlement services in Southern Africa," he explains.

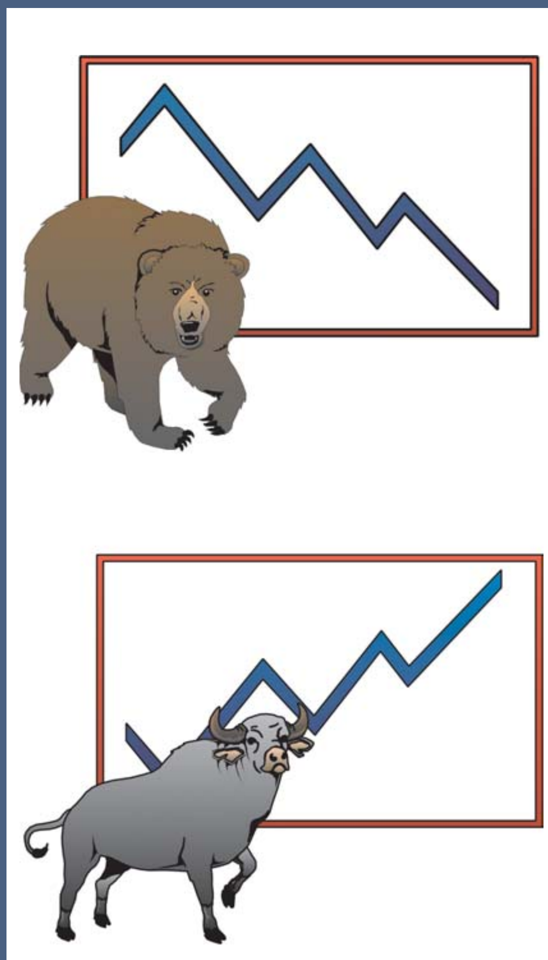
The merged entity will also be responsible for providing the infrastructure and services to cater for the electronic clearing and settlement of dematerialised money market instruments. "It is anticipated that money market instruments will go electronic in the second half of 2004 and that paper-based instruments will gradually disappear. This will reduce the risks of theft, forgery and failed settlements," he says.

An application to approve the proposed merger between STRATE, CD and Unexcor has been submitted to the FSB. "We are processing this application," he says.

JSE to launch small cap stock market

The JSE Securities Exchange South Africa (JSE) plans to launch a new small cap stock market in October 2003, to be called the Alternative Exchange (Alt^{X}).

"This is a market for small to medium companies that are in a growth phase. Alt^{X} will run in parallel with the JSE's main board and will eventually replace the Venture Capital Market and the Development Capital Market," says Norman Müller, FSB's head: Capital Markets.



Alt^{X} will save many small cap firms from being forced to delist due to the high costs of maintaining a JSE listing.

"The listings requirements for Alt^{X} have been finalised. Issuers wishing to apply for a listing on this exchange must comply with, among others, the following requirements," says Müller:

* Issuers must appoint a designated adviser.
* The company must have share capital of at least R2m.
* No profit history is required by the company.
* The public must hold a minimum of 10% of each class of equity shares and the number of public shareholders must be at least 100.
* The directors must have completed the Alt^{X} Directors Induction Programme or must make arrangements to the satisfaction of the JSE to complete it.
* The company must appoint an executive financial director with the appropriate expertise and experience.
* At least 25% of the directors must be non-executive.

A number of benefits will arise from the implementation of Alt^{X}.

It will -

* create a springboard for small/ medium enterprises to list and eventually migrate to the main board;
* stimulate market participation;
* develop directors' skills and thereby improve corporate governance and perceptions of SMEs; and
* create an alternative mechanism for savings and wealth creation and distribution.

"In line with international experience, strong branding and extensive marketing of this market will be a key requirement for maintaining high levels of investor and participant interest", adds Müller.

JSE launches stock exchange financial literacy board game

The JSE Securities Exchange South Africa (JSE) has joined Karina Strydom and Smile Education systems to develop, produce, market and sell a stock exchange financial literacy board game for children from pre to secondary school levels. The game will be known as "Running with Bulls."

Sydney Maree, Director: Marketing and Communications of the JSE and FSB Board Member said the game will provide a real means to demystify the JSE and educate future and current investors about the stock exchange and how to invest on it.

"In some countries, 50% of the population invests directly in companies by purchasing shares as this is part of their economic culture. However, in South Africa, a very small percentage of the population is directly involved with such investments. We are looking forward to the Running with Bulls game starting to change this," he said.

Strydom, inventor of the game, said that it has been especially designed to create a fun-filled environment in which younger people can learn the fundamentals of the stock market. "For children to understand the concept of saving and investing they have to do it themselves," she explains.

Smile Education Systems will develop and market the game. Louise Barclay, managing director of the company, said they are very excited by the opportunity to create an interest in stock markets, particularly among people who would not previously have been exposed to it.

Source:
JSE Media Release,
24 April 2003

JSE and DTI to promote South African Women's Enterprise Network

The JSE Securities Exchange South Africa (JSE) and the Department of Trade and Industry (DTI) will jointly promote the South African Women's Enterprise Network (SAWEN).

"Equality in South African business will never be fully achieved if women do not understand the workings of stock, commodity and bond markets, the operations of the JSE Securities Exchange South Africa and how to engage with these markets and institutions," said Lindiwe Hendricks, Deputy Minister, Department of Trade and Industry.

"The Memorandum of Understanding (MOU) between the JSE and SAWEN outlines the need for women entrepreneurs to receive training in these areas and commits the JSE to offer such training. It will be incumbent on the leadership of SAWEN to ensure that women entrepreneurs are informed about such training."

The DTI and JSE have agreed to enter into an MOU to engage women in initiatives to strengthen and support their own enterprises. The parties will co-operate and assist each other in training and the sharing of information to make the SAWEN programme successful. The JSE is supportive of the DTI's SAWEN plan. "Women are starting to find their feet in business, and this initiative will help guide and focus their efforts," said Nicky Newton-King, the JSE's deputy chief executive officer.

Source:
JSE Media Release, 29 April 2003

FSB hosts meeting of the IOSCO Africa/Middle East Regional Committee

By Norman Müller, head: Capital Markets, FSB

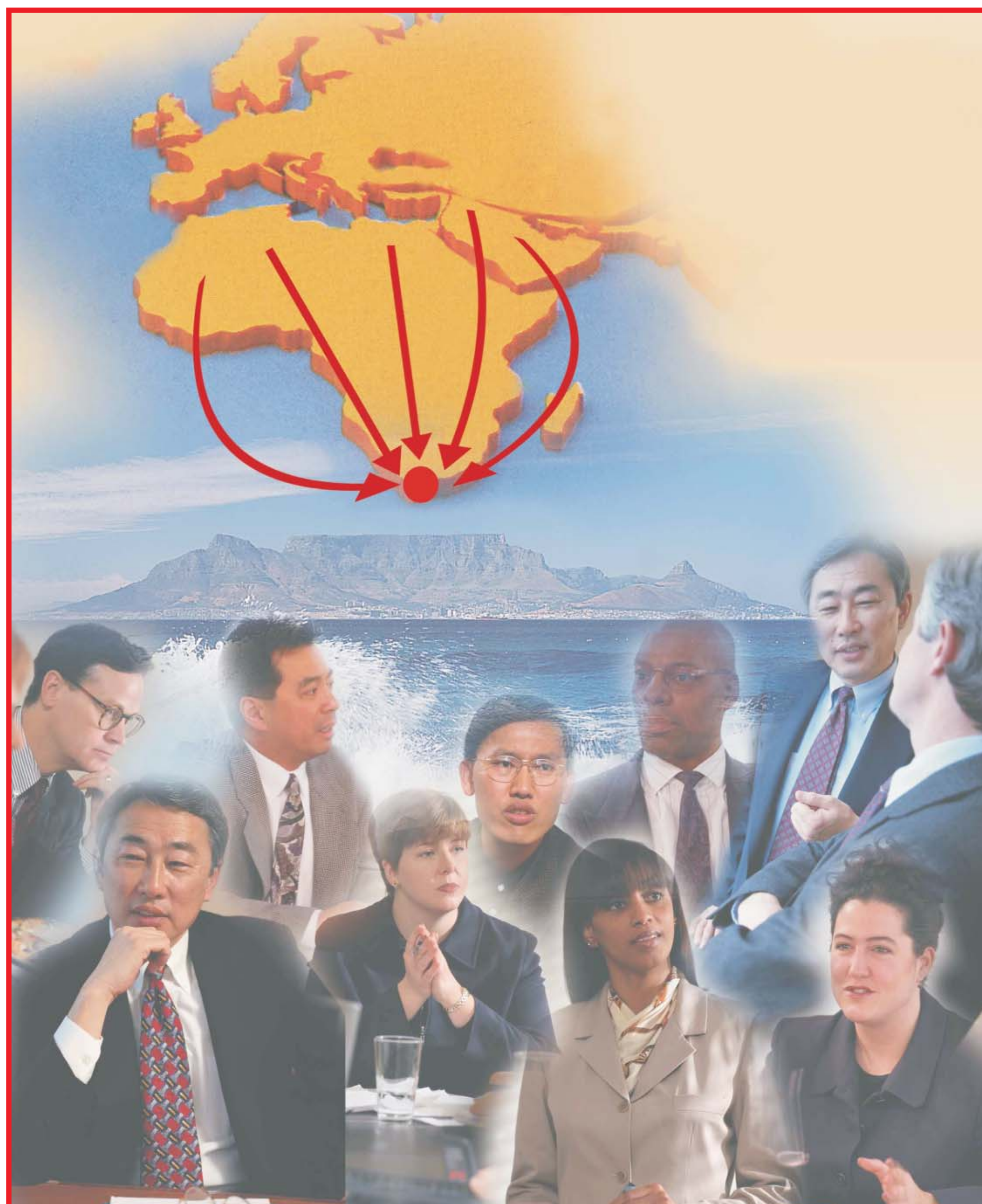
For the first time in the International Organisation of Securities Commission's (IOSCO's) history, the Africa/Middle East Regional Committee met separately from the IOSCO Annual Conference.

Due to the unstable situation in Jordan, who would have hosted the meeting, South Africa was requested to arrange it at short notice. The FSB hosted the meeting in Cape Town on 8 and 9 May 2003. The meeting was successful with complimentary feedback from delegates.

Apart from the opportunity African and Middle Eastern regulators had of getting to know one another and strengthening ties, a number of important matters were discussed.

Isabel Pastor of the IOSCO Secretariat made a presentation on the process, procedures and requirements to become a signatory to the IOSCO Multilateral Memorandum of Understanding (MOU). She also informed members of the technical assistance that the Secretariat provides to applicants. The approval of the FSB's application to become a signatory to IOSCO's Multilateral MOU is expected to be announced at the next annual convention in Seoul, during October 2003. This will confirm that FSB legislation regarding capital markets is modern, up-to-date and in line with international best practice.

The last three IOSCO self-assessment questionnaires on securities regulation, i.e. on secondary securities markets, market intermediaries and collective investment schemes, were due for completion at the end of December 2002. Members discussed their experiences and difficulties in completing these questionnaires.



Andrea Corcoran of the Commodity Futures Trading Commission of the United States made a presentation on the status of IOSCO's benchmarking exercise regarding the IOSCO objectives and principles of securities regulation. The benchmarking document will be released soon to members and will assist them to determine whether they are in compliance with the 30 IOSCO principles of securities regulation.

Members were invited to comment on the three draft papers of the Technical Committee of IOSCO, which will be tabled for endorsement by IOSCO's Presidents' Committee. The papers deal with the following subjects:

* Principles of auditor independence and the role of corporate governance in monitoring an auditor's independence;
* Principles for auditor oversight;
* Principles for ongoing disclosure and material development reporting by listed entities.

As there is a great desire to improve the regulatory skills of regulators, training needs in the African region were analysed. Robert Smith of First Initiative, an affiliate of the World Bank/IMF, gave a presentation on the role his organisation could fulfil in providing funding for certain qualifying projects, including training initiatives.

The next Africa/Middle East Regional Committee Meeting will coincide with the annual conference of IOSCO in October.

CISNA on the go

The South African Development Community's (SADC) Committee for Insurance, Securities and Non-banking Financial Authorities (CISNA) held its seventh meeting in Maputo, Mozambique during April 2003. Twelve of the 14 member countries attended the meeting, as well as representatives of the World Bank, IMF, First Initiative, SADC Secretariat and Eastern Africa Securities Regulatory Authorities.
Since CISNA's last meeting, progress has been made regarding the signing of its Multilateral Memorandum of Understanding (MMOU) on the Exchange of Information and Surveillance of Securities, Insurance and Retirement Activities as well as assistance with training projects.

One of the highlights of the meeting was when the Financial Services Commission of Mauritius and the Bank of Mozambique signed the CISNA MMOU. "Only three regulatory authorities still need to sign this MMOU," says Norman Müller, FSB's head of Capital Markets.

"It is the intention to prepare another CISNA MMOU which will focus on the aims and objectives of CISNA and areas of cooperation between the SADC non-banking financial regulatory authorities, with the aim of facilitating the implementation of the strategy of CISNA. This will be in line with other MOUs of committees within the SADC structure," explains Müller.

As SADC is regorganising, its secretariat gave a brief overview on its restructuring.

CISNA's Implementation and Monitoring Framework had been amended to reflect the progress made since its meeting in October 2002. Most countries have now submitted their individual country's Monitoring Frameworks to the CISNA secretariat.

CISNA's ongoing efforts to contact organisations to assist with its training projects and the establishment of a permanent secretariat, started to pay off. Robert Woodbridge and Cristina Bortes, representatives of FIRST Initiative, made a presentation on the objectives of FIRST Initiative and provided information on the types of projects they focus on. They were keen to explore ways in which they can support CISNA with its projects.

"The Capital Markets and Insurance sub-committees of CISNA made good progress on their respective action plans, as outlined in CISNA's Strategic Plan," says Müller.

The following presentations on topical issues were made:

* Pedro Barreto of KPMG, Mozambique made a presentation on "An International Perspective on Incorrect Financial Reporting".
* Michael Fuchs of the World Bank and Alain Ize of the International Monetary Fund made a presentation on "What a supervisory authority should know about the World Bank/IMF country analysis - FSAP (Financial Sector Assessment Programme)".
* Samantha Anderson, Director of Financial Markets of the National Treasury of South Africa, made a presentation on "The Future of Regulation – can we stop playing catch-up all the time?"

The next meeting will take place in Luanda, Angola on 30 and 31 October 2003.

FSB serves on African insurance regulatory organisations

Deon van Staden, FSB's head: Registration and Policy represents the FSB on AAISA and AIO.

The FSB has been elected to the executive committee of the Association of African Insurance Supervisory Authorities (AAISA) and has been appointed as the Secretary-General and Treasurer of AAISA at its executive committee meeting in Livingstone, Zambia recently.

AAISA is the umbrella body which brings together insurance supervisory authorities throughout Africa. "Its main objectives are to promote co-operation among supervisory authorities, to assist countries in human resources development, and to create a forum for the standardisation of insurance laws and supervisory structures on the continent," explains Deon van Staden, FSB's head: Registration and Policy. "It is also a forum for African regulators to discuss issues of mutual concern. Fifty-three regulators are AAISA members," he adds.

The FSB is also a member of the African Insurance Organisation (AIO) and was appointed a member of its Credit Assessment Committee (CAC). "The CAC is supported by the United Nations Conference on Trade and Development (UNCTAD) and the credit rating companies, Standard and Poors and AM Best.

"AIO's main aims are to promote co-operation between members, as well as the development of a healthy African insurance and reinsurance industry. The committee's main activities include the annual African Insurance Conference, organising of seminars and workshops, the publishing of the African Insurance Annual Review, as well as the establishment of the African Aviation Pool and the African Oil and Energy Insurance Pool."

Shares in holding companies

From p.11

From p.11

Where to from here?

The pending Insurance Amendment Act, which is expected to be promulgated in the second half of 2003, will insert the following new provision in the 1998 Act, as section 34(1)(e):

"A long-term insurer shall not **include in its assets shares held directly or indirectly in its holding company**, without the approval of the Registrar, given generally or in a particular case, and subject to such conditions as the Registrar may determine."

There is some uncertainty as to whether section 34(1)(e) will apply also to shares in its holding company that an insurer holds in its policyholder funds. Section 32(2) already provides that an insurer may not, in its policyholder funds, hold shares in its holding company without the approval of the Registrar and subject to such conditions the Registrar may determine.

The only differences between section 34(1)(e) and section 32(2) are:

* Section 34(1)(e) refers to shares held "directly and indirectly" in the holding company, where section 32(2) does not.
* Section 34(1)(e) says the approval by the Registrar can be given "generally or in a particular case", where section 32(2) does not.
* Section 32(2) refers to the "prior" approval of the Registrar, where section 34(1)(e) does not.

A court probably will interpret the position along the following lines: Section 32(2) is an existing, special provision that already deals specifically with shares in its holding company held by an insurer in its policyholder funds. Section 34(1)(e) is a later, additional provision that deals generally with shares held by the insurer in its holding company. One basic rule of interpretation is that general provisions must be taken as not to detract from special provisions. This rule requires, among others, that a later enactment [section 34(1)(e)], which deals with a subject generally, be construed in such a way that it does not detract from the validity of an earlier enactment [section 32(2)], which deals with that subject specifically - except if the later general enactment proves to be an exhaustive codification of that subject.

It is clear that section 34(1)(e) is not such an exhaustive codification. Therefore, it is meant to apply only to shares held by an insurer in its holding company, to which section 32(2) does not already apply.

If this interpretation is correct, the legal position, after section 34(1)(e) has come into being, will be as follows:

An insurer may, under section 32(2), in its policyholder funds, hold up to 100% of the shares in its holding company, subject to the limit the Registrar may place on this shareholding in terms of section 32(2)(b). Presently, as mentioned above, the Registrar requires, for an insurer who applied for approval after the 1999 amendment, that the shares in its holding company that it holds in its policyholder funds, together with the shares in its holding company that it holds in its shareholder fund, and together with the shares in its holding company held by other subsidiaries of its holding company, be not more than 10% of the issued shares in its holding company.

An insurer may, under section 89, in its shareholder fund, hold up to 10% of the shares in its holding company, subject to the limit the Registrar may place on this shareholding in terms of section 34(1)(e). The Registrar is expected to require that the shares in its holding company that an insurer holds in its shareholder fund, together with the shares in its holding company that the insurer holds in its policyholder funds, and together with the shares in its holding company held by other subsidiaries of its holding company, be not more than 10% of the issued shares in its holding company. (See table below)

The valuation of the assets of long-term insurers

In future insurers will have to value their assets (and liabilities) by means of the so-called statutory valuation method. This method is set out in the new Schedule 3 to be inserted in the 1998 Act by the pending Insurance Amendment Act.

The new Schedule 3 requires that the valuation be done also in accordance with supplementary requirements to be prescribed by the Registrar ("the prescribed valuation requirements").

The prescribed valuation requirements will limit the value an insurer may place on shares it holds in its holding company. The current proposal is that, if its holding company is listed, the value of the shares in its holding company may not be more than 5% of the value of the total liabilities of the insurer. If its holding company is not listed, the value of the shares in its holding company must be taken as nil.

The upshot of this is that an insurer may, for valuation purposes, take into account only so much of the shares it holds in its holding company as is permitted from time to time by the prescribed valuation requirements, irrespective of the number of shares it holds in its holding company under section 89 and section 32(2).

Summary of the position after section 34(1)(e) has come into being

Shares an insurer may hold in its holding company - in its shareholder fund	**Shares an insurer may hold in its holding company - in its policyholder funds**
General position - sections 89, 39(1), and 34(1)(e) * up to 10% - but limited by the Registrar to so many as will, together with the shares in its holding company held by the insurer in its policyholder funds, and together with the shares in its holding company held by other subsidiaries, be not more than 10% of the issued shares in its holding company * no voting rights	General position - shares deemed to be held as trustee - section 32(2) * up to 100% - but limited by the Registrar, for an insurer who applied for approval after the 1999 amendment, to so many as will, together with the shares in its holding company held by the insurer in its shareholder fund, and together with the shares in its holding company held by other subsidiaries, be not more than 10% of the issued shares in its holding company * no voting rights
Shares acquired before the insurer became a subsidiary of its holding company Position now uncertain	Shares acquired before the insurer became a subsidiary of its holding company As under general position above - section 32(2)

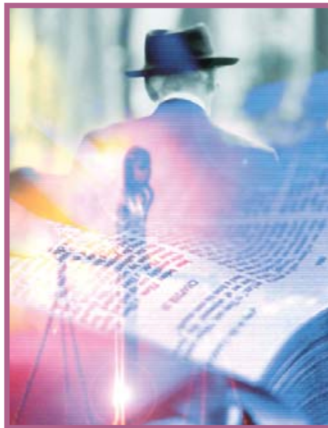
Pepkor

From p.3

'reasonable and equitable'. In the court's view, if the Registrar were to conclude that the proposed transaction was neither just, nor equitable, because the funding level of the transferring fund considerably exceeded the funding level of the transferee funds and there was a substantial surplus which would remain in the transferring fund, he would be acting fully within his regulatory powers and a court would not on review be able to interfere with his decision simply because it did not agree with it.

If the Fund should be liquidated (as it has been) transferring members would have some prospect of sharing in a surplus should one exist (as it does) - not because they had an existing legal right to do so, but because some arrangement would have to be made to deal with the surplus.

It was pointed out that a public functionary may be entitled and even obliged to seek the review by a court of its own decision. The Registrar and the FSB are entitled to do so. The question which then arises is whether this should be permitted because of a material mistake of fact, even a mistake due to the functionary's own negligence (which the appellants submit was present in this case in as much as, according to the appellants, the Registrar should have realised that the information provided by Meyer could not have been correct and should have made further inquiries) and even if the mistake was not induced by the person who benefited by the decision.



Hitherto, where jurisdiction is not in issue and there is no obvious transgression of the boundaries within which the functionary has been empowered to make decisions, our courts have not permitted a review solely on the basis of a material mistake of fact on the part of the person who made the decision.

Judicial intervention has been limited to cases where the decision was arrived at arbitrarily, capriciously or *mala fide* or as a result of unwarranted adherence to a fixed principle or in order to further an ulterior or improper purpose; or where the functionary misconceived the nature of the discretion conferred upon him and took into account irrelevant considerations or ignored relevant ones; or where the decision of the functionary was so grossly unreasonable as to warrant the inference that he had failed to apply his mind to the matter. The court took the view that a material mistake of fact should be a basis upon which a court can review an administrative decision. If legislation has empowered a functionary to make a decision, in the public interest, the decision should be made on the material facts which should have been available for the decision properly to be made. And if a decision has been made in ignorance of facts material to the decision and which therefore should have been before the functionary, the decision should be reviewable at the suit of *inter alia* the functionary who made it - even although the functionary may have been guilty of negligence and even where a person who is not guilty of fraudulent conduct has benefited by the decision.

The judge found that the Registrar was misled on a fact material to his decision. There was no prejudice to Pepkor Limited, sufficient to warrant denial of the relief: the effect of the relief will be potentially to deny to it a windfall which it could not legitimately have expected and to which it has never become entitled. Nor can there be any question of prejudice to the Fund. On behalf of the appellants it was submitted that it would be 'practically unworkable and legally indefensible to undo the transfers at this late stage'. The SCA, however, dismissed the appeal against the setting aside on review of the section 14 certificates and the resultant transfers of money from the fund to the 'daughter' funds, and from the 'daughter' funds to the defined contribution funds.

The SCA did not consider that the appellants' limited success in challenging the *locus standi* of the FSB to require repayment of the R9,2m was a reason for depriving the FSB of any part of its costs.

Commenting on the case, Adv Dube Tshidi, FSB's deputy executive officer: Retirement Funds and Friendly Societies, said that serious negotiations will still take place before the final chapter in this saga is written.

FSB trains its staff on Financial Intelligence Centre Act

By Martin Dzviti, head: Inspectorate, FSB

Ongoing joint training of staff of the FSB, South African Reserve Bank (SARB) and South African Revenue Services is taking place at the SARB training college. Staff members are being trained in awareness, identifying and reporting suspicious transactions. "We have received some recommendations from students and are reviewing the syllabus to enrich it," says Martin Dzviti, Head of the FSB's Inspectorate.

The FSB is working with the industry to draft guidelines for compliance by accountable institutions with the money laundering control measures. The FSB's Financial Intelligence Centre Steering Committee has consulted with various industry bodies and consensus on a single set of guidelines for the whole industry has been reached. Workshops to finalise the guidelines are planned.

FSB participates in "Take a girl child to work" initiative

By Thandile Makubalo, manager: Formal Education, Consumer Education, FSB

During May, the Consumer Education Department co-ordinated the FSB's participation in Cell C's "Take a Girl Child to Work" initiative. The programme was aimed at involving business, government and the public in focused collaborative action to reverse gender stereotyping in South Africa. The FSB hosted eight girls and participated in the proceedings at the Sandton Convention Centre. The girls had lunch at the FSB, after which people from various departments gave short presentations on the functions of their respective departments. They also offered career guidance advice. This event highlighted the need for community outreach programmes.

The FSB hosted eight girls as part of the "Take a Girl Child to Work" initiative. Thandile Makubalo (front row, far left), Kedibone Dikokwe (centre - front) and Ntombi Mahlangu (next to Kedibone) from the FSB ensured that the girls had a memorable day.

Handbook of International Auditing, Assurance, and Ethics Pronouncements

Reviewed by Willemien de Jager, project manager, Prudential Insurance, FSB

This handbook brings together background information about the International Federation of Accountants (IFAC) and the effective pronouncements on Auditing, Assurance, and Ethics issued by IFAC as of 1 January 2003.

IFAC is the worldwide organisation for the accountancy profession. Founded in 1977, its mission is to develop and enhance the profession with harmonised standards, to enable it to provide services of consistently high quality in the public interest.

The handbook is arranged as follows:

* Changes of substance from the 2001 edition of the handbook and recent developments
* Ethics
* Auditing and Assurance
* Statement of Policy of Council – Recognition of Professional Accountancy Qualifications
* International Professional Practice Statement 1- Assuring the Quality of Professional Services

With the scandals in the auditing and accounting profession over the last few years, it is important for the regulator to keep abreast with the latest developments in the auditing world. The regulator needs to ensure that his reliance on the auditor is in accordance with international developments.

The handbook can be viewed at *www.ifac.org*.

Where does money laundering occur?

As money laundering is a necessary consequence of almost all profit generating crime, it can occur anywhere. Generally, money launderers tend to seek out areas in which there is a low risk of detection due to weak or ineffective anti-money laundering programmes. Because the aim of money laundering is to get the illegal funds back to the individual who generated them, launderers usually prefer to move funds through areas with stable financial systems.

Money laundering activity may also be concentrated geographically according to the stage the laundered funds have reached. At the placement stage, for example, the funds are usually processed relatively close to the underlying activity; often, but not in every case, in the country where the funds originate.

With the layering phase, the launderer might choose an offshore financial centre, a large regional business centre, or a world banking centre - any location that provides an adequate financial or business infrastructure. At this stage, the laundered funds may also only transit bank accounts at various locations where this can be done without leaving traces of their source or ultimate destination.

Finally, at the integration phase, launderers might choose to invest laundered funds in other locations if they were generated in unstable economies or locations offering limited investment opportunities.

Source: FATF Website