INAUGURAL
INDUSTRY WIDE
CONFERENCE
SPECIAL EDITION

FSCA NEWSLETTER

June 2024

FSCA
Financial Sector
Conduct Authority

THE CON TENT

Q1 Newsletter

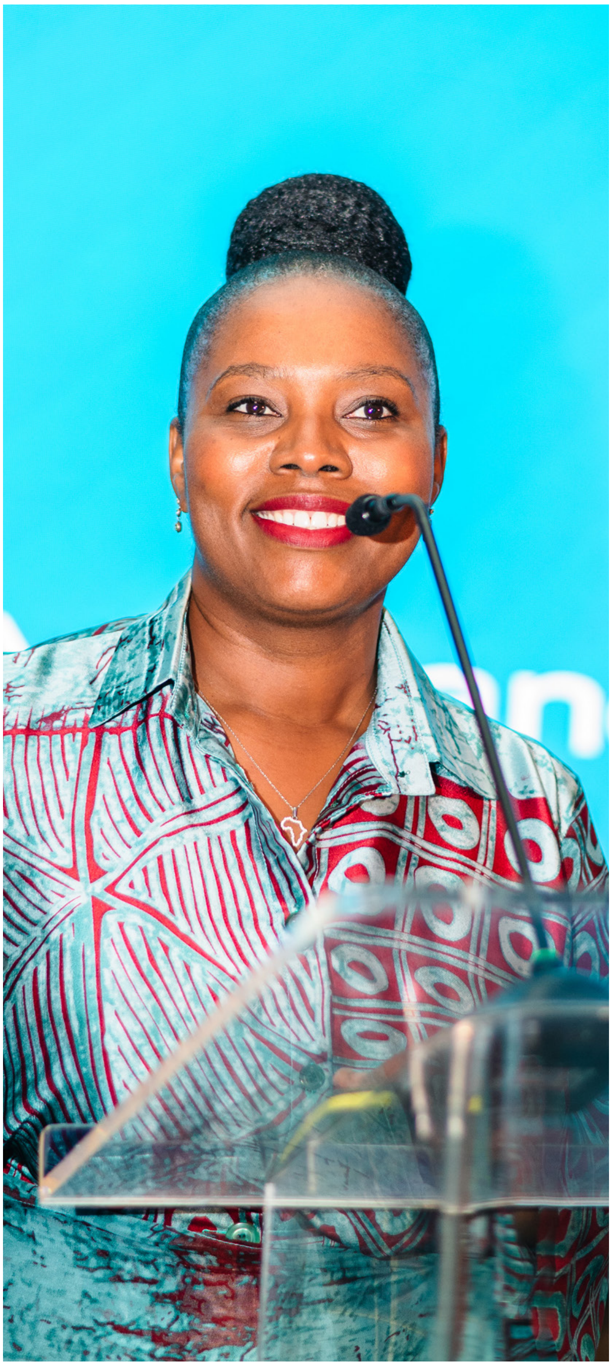
EDITOR'S NOTE

In March this year we held our inaugural FSCA industry wide conference, centred around the theme of inspiring trust in our sector. While we've hosted conferences/seminars/workshops over the years, this was the first time that the Authority gathered representatives from across the financial sector to discuss cross-cutting issues. What was imperative for us in these discussions was for the conference not to be a one-sided flow of information, but rather a meaningful dialogue that could capture both our thoughts and sentiments, as well as those of industry players.

The panel discussion topics were carefully crafted to create an opportunity for all of us to reflect meaningfully on key areas that affect businesses and customers in our sector.

What a resounding success the conference was! Our sincerest thanks to everyone that attended. In this edition of our newsletter, we walk you through the pivotal points of the conference and provide you an opportunity to reflect on these all-important discussions.

Best wishes,
Tembisa Marele



FSCA
INAUGURAL INDUSTRY WIDE CONFERENCE 2024

COMMISSIONER KAMLANA'S

Opening Remarks (Full Speech)

Good morning, ladies and gentlemen.

Thank you so very much for making the time to come out here and welcome to our industry-wide conference. We are looking forward to engaging in great and insightful conversations about our work, and our role and getting an understanding of developments pertaining to the financial sector.

I wish to extend a special welcome to Mr. Lesetja Kganyago, the Governor of the South African Reserve Bank, the 10th Governor of our central bank. Thank you very much for honoring our invitation and we are also looking forward to your keynote address later.

Let me offer a few contextual remarks, intended to frame the discussions over the next day and a half and position the strategic importance of this engagement in terms of the work programme of the FSCA and our mandate.

If I would try and suggest the key phenomena which have characterized the state of the South African financial sector in recent times, from a conduct perspective:

The first issue would be the cost-of-living crisis and the increasing vulnerability of consumers (Governor, no pressure for your meeting with the MPC later this month), but really what do we see and how do we think about the role of financial institutions in that context. So that's the first issue.

The second issue, which could have easily been the first, it's this issue of market integrity – the need for us for get ourselves off the FATF greylist – and to do so within the agreed timeframe in terms of the action plan that we have. This issue directly impacts the reputation and credibility of the South African financial sector on the global stage. So, it is urgent.

The third issue, is the structural change that the two pot system represents in terms of retirement savings how we think about retirement savings policy and outcomes and the last issue – is about the theme of this conference, which is about building trust in the financial sector – what is our assessment of where the sector stands in terms of conduct reputation and levels of trust in the sector – and that includes a lot of things, whether you are looking at innovation and how technology is deployed as business models change and evolve, our ability to respond to those changes and deliver on treating customers fairly and all these good things in terms of customer outcomes. The ability of leaders at the highest level in organisations to champion these issues – around culture, governance, accountability, transparency, transformation – all of these contribute to good conduct.

I am mentioning these four – and really don't intend to touch on all of them in my opening remarks – but I certainly hope that we can hear from yourselves about what you think about these issues and how we should work together in addressing them.

FSCA Commissioner
Unathi Kamlana

The cost of living crisis

On the cost of living crisis the issue of interest for us is the increasing vulnerability and fragility of households, with many struggling to cope with the rising costs of basic necessities. How's the sector thinking about this and is the response adequate – it's an issue to debate and agree an approach.

It's also about levels of household debt, it's about debt service costs, what financial products are sacrificed in order for people to make ends meet, as industry your role becomes even more crucial in this context.

South Africa grey-listing

Then on the issue of the grey-listing, I guess the central question is are we doing enough, all of us – to get our country off the greylist timeously. Many jurisdictions have been able to get themselves off, will we be able to, given the economic cost of this. Some of you have been on the receiving end of our actions as we try to address FATF recommendations. Just to say that those who have not yet been affected – your letters are in the mail. Coming to a letter box near you.

But seriously, the message about this is that it is a collaborative effort and Treasury is leading us on this and we are all doing our part.

Retirement Funds Two-Pot system

Historically, retirement funds have focused on long-term savings accumulation, with limited access before retirement, aiming to secure a substantial financial base for individuals' retirement years. However, this approach often left members without an immediate financial safety net, leading to premature withdrawals that could compromise their long-term financial health and retirement readiness. To address these challenges, the two-pot system introduces a flexible framework allowing for emergency access to a portion of savings without endangering future retirement security. This change aims to enhance member trust and engagement by providing a balance between immediate financial needs and long-term savings objectives. As regulators, we are actively collaborating with the industry to ensure seamless implementation of this system.

Our approach is both capacity to deal with rule amendments in the short term but also to focus on education in order to enhance member outcomes. The second part of the reforms – which talks to compulsory preservation should also have adequate coverage in terms of the conversation.

The Importance of trust in the financial sector

So let me come to this issue of levels of trust in the sector. Firstly, I raise this because trust is an essential ingredient of something more important that is necessary in the sector – and that is confidence and that's essential for another important thing – that is stability. So, I would really be interested in hearing what is your view of the levels of trust in the sector and what can be done to improve it. We have chosen this focus as a theme because of it's strategic importance for our work as the FSCA – it's fundamental, it's foundational for the entire system and how it operates. The scandals and the reputational knocks that the sector takes are not helpful – to be clear. We need to take proactive measures to uphold and rebuild trust.

Leadership and Culture

Leadership and culture are at the centre of it. It doesn't help when we have scandals around the integrity and qualifications of leaders and their credibility. We must talk about this and resolve it. Tone from the top – there's no other way.

In collaboration with the Prudential Authority, we are developing a joint standard on culture and governance. This standard will set the benchmark for ethical behavior and leadership accountability, ensuring that these critical elements are consistently upheld across the sector. The draft Joint Standard is going through targeted industry consultation, which will be followed by formal public consultation.

Reflection on the FSCA's Journey

As an organisation, we celebrated our fifth anniversary last year. Over that period, we have undergone a profound transformation, guided by the principles of the Twin Peaks model—a framework that has shaped our approach to financial regulation. Embracing both the opportunities and challenges presented by this new regulatory landscape, we have implemented strategies and initiatives to promote fair customer treatment and ensure the efficiency and integrity of financial markets.

We have moved beyond mere compliance-based approaches to proactive risk identification and mitigation. To outcomes- and principles-based regulation and supervision, focusing on fair customer outcomes rather than prescribing detailed rules. This approach allows you as the sector, the flexibility to design their products and services to meet customer needs within the overarching principles set by us.

Recognising the evolving landscape of financial technology, we established an internal Fintech department to ensure we remain at the forefront of developments and drive responsible innovation. Playing a crucial role in providing thought leadership on emerging innovations in the sector and has made significant contributions to the work of the Intergovernmental Fintech Working Group (IFWG). Since its establishment, the department has published several papers, including a Position Paper on open finance and the most recent report on a crypto assets market study. These have helped our inrail approach to regulating crypto assets.

Furthermore, our digital transformation journey began with the launch of our Digital Transformation Strategy, a critical step towards becoming a more agile, innovative, and digitally savvy organisation. We have recently acquired an Integrated Regulatory System that will enable us to understand conduct risks more holistically across regulated entities and enhance our regulatory oversight capabilities. This system will streamline processes and improve collaboration by providing a centralised platform for sharing information and coordinating efforts.

Looking Ahead: Challenges and Opportunities

Technology innovation and associated risks

These advancements also come with significant risks, such as cybercrime and data privacy concerns.

As a regulator, we are concerned about cybersecurity risks associated with technological advancements. These risks can undermine trust and stability in the financial sector, leading to substantial financial losses, eroding customer confidence, and disrupting essential financial services. In response, we, in collaboration with the Prudential Authority, will be making a joint standard on cybersecurity to ensure financial institutions implement robust measures and resilience strategies. The critical nature of this issue requires us to remain vigilant and proactive in ensuring the financial system's resilience against evolving cyber threats.

Artificial Intelligence, another topic we will tackle here today, has emerged as a significant innovation poised to redefine the financial services industry, promising efficiencies and new capabilities. Acknowledging the significant implications of AI, we will conduct a market study this year on its impact on financial services. This study will explore the potential benefits and associated risks, ensuring that as we embrace AI's advancements, we maintain a balance between innovation and the safeguarding of customers and the integrity of our sector.

Conduct of Financial Institutions (CoFI) Bill

The forthcoming Conduct of Financial Institutions (CoFI) Bill is set to enhance our regulatory approach further, enabling agile responses to cross-sector risks through conduct standards. The CoFI Bill, currently being finalised by National Treasury before proceeding to Parliament, is a significant step in reforming the conduct regulatory framework by consolidating various financial sector conduct laws into a single legislation. Anticipating the significant changes, the CoFI Bill will bring, we are not waiting for its official enactment to adjust our frameworks and processes. Instead, we are proactively aligning our current practices with the Bill's principles to ensure a smooth transition, thereby minimizing disruptions and maximizing benefits for both consumers and the industry.

Financial markets legislative reform

As we proactively prepare for the implementation of the CoFI Bill, our focus on legislative reform extends beyond conduct of financial institutions to encompass financial markets. We are also working with National Treasury, Prudential Authority, and other stakeholders to reform South Africa's financial markets' legislative framework based on proposals outlined in the National Treasury's policy paper released in March 2020, titled "Building Competitive Financial Markets for Innovation and Growth". These proposals include a move from a purely self-regulatory model to a shared responsibility, with the FSCA taking greater oversight responsibility, especially in the area of cross market surveillance. We are currently exploring and evaluating these proposals to determine the most effective way to implement them.

In preparation for assuming greater oversight responsibilities, we are enhancing our capacity for market oversight and surveillance, especially in over-the-counter and fragmented exchange-traded markets. This will involve the licensing and development of a trade repository for central data collection, analysis, and monitoring of trends. These reforms, which also stem from the recent IMF Financial Sector Assessment Program, will help ensure that the FSCA is fully equipped to detect and prevent market manipulation and insider trading.

Furthermore, we have been working on a Conduct Standard for Market Infrastructures, which will be published for public consultation in due course. Through this conduct standard, we aim to ensure that a level playing field is established among market infrastructures.

Promoting sustainability

Governance and culture are essential foundations for promoting sustainability within the financial sector, providing the structure, values, and incentives necessary to integrate sustainability considerations into business practices effectively. In an era of increased concerns over climate change, social inequality, and governance challenges, we are proactively positioning ourselves to play an active role in enabling a financial sector that supports sustainable objectives. In this regard, we have taken a significant step forward by publishing our introductory Statement on Sustainable Finance and program of work. This publication outlines the FSCA's plan to cultivate a financial sector that is not only fair, efficient, and resilient but also supports inclusive and sustainable development. As a market conduct regulator, it is clear that the FSCA has a vital role to play in improving the availability of credible and consistent information in the South African financial markets. The program of work underway includes promoting the adoption of a common taxonomy for sustainability, aligning disclosure and reporting requirements, and ensuring that customers remain protected against risks of greenwashing, social washing, and other risks that may arise as markets for sustainable financial products expand. As an organisation, the FSCA has adopted sustainability as one of our values. We will publish a Sustainable Finance Roadmap in the coming weeks, which will serve as our guiding document in our efforts to promote sustainable finance over the next few years.

Conclusion

As I conclude, let us take a moment to appreciate the journey we have embarked upon together with the sector and with our sister regulators. As we shift our focus to the period ahead, let us embrace the uncertainty with courage and optimism, knowing that each step forward brings new opportunities for learning, collaboration, and innovation.

Over the course of today and half of tomorrow, we are set to explore a multitude of topics, ranging from the FSCA's plans for the period ahead to the challenges posed by the FATF grey-listing, as well as the progress made in exiting the grey list, and the exciting opportunities and risks brought about by technological advancements.

I encourage each one of you to actively participate and engage in the meaningful dialogues that will unfold today and tomorrow. Your insights, questions, and discussions are the key components that will drive the success of this gathering.

Thank you and welcome to the conference. I hope that you will find the discussions rewarding, and the entire conference enjoyable.

At this point, please allow me to invite the Governor to give his keynote address.

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THE GOVERNOR
OF SOUTH AFRICAN RESERVE BANK

Lesetja Kganyago delivers Keynote address on Market conduct and financial stability (Full Speech)

Good morning.

Thank you for inviting me to speak at this inaugural industry-wide Financial Sector Conduct Authority (FSCA) Conference.

My topic today is the relationship between market conduct and financial stability. As you know, these are the Twin Peaks of our new model for financial regulation, which came into force in 2017. This was the same landmark reform that birthed the FSCA as well as the Prudential Authority (PA).

The South African Reserve Bank (SARB), which incorporates the PA, has ultimate responsibility for financial stability. At the same time, the FSCA is the apex authority for market conduct. There is a clear separation.

Our Twin Peaks model has yet to fully mature. For instance, pension funds and collective investment schemes are expected to move to the PA only in April 2026. It is nonetheless a comparatively robust model, especially for a highly concentrated financial sector with a small number of large players, as well as for the continuous development of financial technology.

Still, even with a clear division of labour, the details of how we pursue financial stability and good conduct are more complex, and sometimes confusing. For instance, if you go to the FSCA website, you will find a list of five strategic objectives, and number one is 'ensure the stability of financial markets'.

You might have thought that was the SARB's responsibility, not the FSCA's.

But of course, to protect financial stability and to restore it when a crisis breaks out, the SARB does not operate in isolation. We rely on other authorities such as the National Treasury (NT), the Financial Intelligence Centre (FIC), the National Credit Regulator (NCR) and, of course, the FSCA. Cooperation between these institutions is also institutionalised through the Financial Sector Oversight Committee (FSOC) and the Financial Sector Contingency Forum (FSCF).

Similarly, Twin Peaks clearly assigns market conduct issues to the FSCA, but that hardly means we at the SARB can ignore conduct issues. Indeed, as I shall argue in this speech, financial stability and conduct issues are ultimately connected. A system rife with misconduct will also become unstable.

Before I turn to our South African context and challenges, let me start by delving into global regulatory and conduct issues.

The global narrative on financial regulation changed completely with the global financial crisis (GFC). Before 2008, finance was widely considered an industry where light touch regulation would free smart people to generate astonishing wealth. This narrative had the most traction in the advanced economies. Indeed, financial crises were often portrayed as things that happened in emerging markets, which could usually be blamed on governments. But, of course, the GFC was triggered by events on Wall Street, the very centre of advanced economy finance. And the private sector was plainly guilty of excessive risk-taking and bad judgement.

The lessons of that crisis ushered in totally new narratives on financial sector regulation. I say narratives because there were two – a technocratic version and what we can call a popular or even populist version.

The technocratic part was about re-engineering finance to make another GFC impossible, through changes such as raising bank capital levels and intensifying supervision. Many people here are experts in this complex, jargon-heavy field.

The popular story was quite different. People saw highly paid bankers bring the economy to its knees, causing extensive job losses, and walking away with no jail time and no claw-back of past bonuses. This made a lot of people angry, manifesting in protests like the Occupy Wall Street movement.

The technocratic mindset and the populist mindset are very different, and the two are usually uncomfortable in each other's company.

Populists are often bored and uncomprehending in technocratic conversations, while technocrats usually flounder when they try and do politics.

But the lesson we must take from this is that financial stability is not just an engineering problem.

I do not think it is possible, at least in a democracy, to have a good policy regime for protecting financial stability, if you do not also have an effective regime for regulating conduct. If people feel abused, tricked or betrayed by the financial sector, they are not going to be interested in thoughtful technocratic proposals for obscure variables such as liquidity coverage ratios. Their elected representatives will not be interested either. The political discussion will centre on moral outrage and that will drain the oxygen out of technocratic debates.

You can try and push along with the technocratic work, following global best practice and debating ratios, but sooner or later the political and the technocratic worlds will need each other. You will get crises, and in crises you really need people to work together, across government, the private sector, and also civil society. If you get to that point and trust has been burnt up by misconduct, good luck getting policy right.

We live in difficult times, so the margin for error is small.

There is a very clear upshift in geopolitical tensions in the world. Our headlines are full of war horrors. This is going to be a record year for elections – and some of these election results could be highly disruptive.

We have also experienced the worst global inflation surge in a generation. Just a few years ago the monetary policy debate in the advanced economies was about inflation that was too low, about deflation risk, about tools for providing stimulus when interest rates are as low as they can go. Now we have significantly higher inflation, and although headline numbers are coming down, underlying inflation is still quite sticky. Interest rates are staying higher for longer.

These higher rates are necessary to stabilise inflation. But elevated interest rates also create stress. We have seen some poorer countries, especially in Africa, lose access to global bond markets. And we have seen bank failures. This month marks the one-year anniversaries of the Silicon Valley Bank (SVB) failure in the United States, and the collapse of Credit Suisse

The Governor of South African Reserve Bank
Lesetja Kganyago

– a global systemically important bank – in Switzerland. The example of SVB is especially interesting. It was basically undone by losses on government bond holdings; not exactly risky assets, but assets which necessarily lose value as long-term interest rates rise. There are some rich ironies here. One of the lessons of the 2008 crisis was meant to be that complex derivatives and risky assets were the cause of bank failures. But here we have a failed bank that got in trouble because of its holdings of the world's classic safe asset, and which failed to hedge the risk– in other words, that did not use derivatives. This is a valuable reminder that risk takes many forms, and the conventional wisdom of the last crisis may be misleading for the next one.

Overall, it is fair to say that we live in challenging circumstances.

Here in South Africa, our region is largely peaceful and likely to remain so. But we are not completely insulated from geopolitical confrontations.

Our economy is also not growing, and there are many signs that our living standards are falling. Growth last year was just 0.6%. Since 1994, there have been only four years with worse growth, of which one was the 1998 emerging market crisis, one was the 2009 crisis, and one was the 2020 COVID-19 crisis. The gap between South African growth and world growth is now double its longer-term average. We are falling behind. A big reason for this is that other places have functioning rail networks, ports and electricity.

At the same time, government debt has risen too fast and is now too high. Accordingly, we have lost our sovereign investment-grade credit rating. This is costing us dearly, through higher borrowing costs and lost investment funds.

Furthermore, we are on the Financial Action Task Force (FATF) greylist and have been there for just over a year – since February 2023. We got this 'high risk' designation partly because of poor conduct by institutions and because of the exploitation of vulnerabilities in the existing financial frameworks relating to anti-money laundering regulations. We feel confident that South Africa will be removed from the greylist by the next review date, in 2025, given the fixes we are implementing. But this has been a costly episode for us. The lesson is that joint efforts are required to look after the integrity of South Africa's financial system. We all suffer when this is compromised.

At the same time – despite all this bad news – we must appreciate that our financial system is resilient. The test of a system is how well it handles stress. You never want to see stress. But we have had a lot of it in recent years, and the good news is that the system has largely coped well. Capital buffers have held up. We have not seen a rise in defaults that would indicate irresponsible risky lending, or large-scale ever-greening of loans designed to conceal losses – both problems experienced in various other jurisdictions, where financial systems are a source of vulnerability rather than strength. The ability of the market to get through catastrophic events like COVID-19 has been clearly demonstrated.

Of course, there are also problem cases, such as certain institutions which we put into curatorship recently. But I think those actions should be interpreted as vigilance, mitigating problems before they grow too large. In a well-regulated financial system, you are more likely to see banks being closed from time to time, rather than dysfunction being tolerated indefinitely.

Unfortunately, we cannot say the public image of the financial sector is everything it should be. It was remarkable, with the allegations last year about banks manipulating the exchange rate of the rand, how ready people were to believe that there was in fact a giant conspiracy to rig the rand, and that this had seriously weakened the exchange rate, pushed up inflation and raised interest rates.

Economists and market specialists understood that even if there had been market manipulation by some traders, the macro effects of the exchange rate being a few cents weaker or stronger for an hour or so would have been trivial. The impact on inflation and rates would have been zero. We also saw the Competition Appeal Court rule in January that there was no evidence of a general conspiracy. But this was not the conversation taking place in the public domain. Most people could tell that traders were behaving unethically, plotting in chat rooms, and this misconduct was so obviously wrong, it eclipsed further analysis.

What I learnt from this is that public trust in the financial system is not as deep as it needs to be. I worry about our ability to have well-informed policy conversations, in potentially more stressful circumstances, if bad analysis can get this kind of public reaction.

Effort to bolster consumer education on the intricacies of financial regulation or financial economics are ongoing. But many people have strong opinions on the ethical questions, and especially the ethical failures. This is the stuff that can catch fire with the public. If one of these fires start, it is going to be a very difficult conversation to control, and a very difficult environment for making policy.

The solution here is the solution with all fire risk: you need to reduce the supply of flammable material, you need early detection systems, and you need firefighting equipment. For our purposes, this means you need to have a financial system which treats people fairly, where misdeeds are detected, and are then dealt with promptly and effectively. If you do not have this, the system will be fundamentally unsafe.

Ultimately, your moral capital is like your financial capital. You need it most in a crisis, and if you do not have it, that is when you fail.

You, the FSCA, are the guardians of the financial sector's moral capital. I do not know how you devise a capital adequacy ratio to measure whether we have enough – but let us have no doubt, even if we cannot measure it, this trust is every bit as valuable as financial capital. So even though we are at the top of two different peaks, you lead on market conduct, and we lead on financial stability, and we need each other to succeed.

Thank you.

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FSCA CONFERENCE DEPUTY COMMISSIONER DIALOGUE

Meet the facilitator, Amanda Khoza

Amanda Khoza has worked for 25 years in accounting, asset management, research, transformation and socio-economic development programmes in the financial services sector. She is the Managing Director Root Kauz Konsult, a management consulting company that she founded. Her directorships include being the Vice President of the Institute of Retirement Funds Africa (IRFA) and Chair of IRFA's transformation & sustainability, and investment practices committees. She is an independent trustee of the Discovery Umbrella and Retail Funds, and an investment committee member. At Efficient Group, she is a board member, member of the investment committee, chair of the remuneration, social and ethics committee, and board member of the Efficient Corporate Solutions business. She also holds a board position at Prime Investments, and is a member of FedGroup's investment committee.

She holds an MBA in finance and strategy focusing on financial inclusion, a Master of Management in Finance and Investment focused on impact and sustainable investing, and is currently pursuing a Masters in Development Finance, focused on ESG integration and sustainable investing. She is a financial services enthusiast who believes financial inclusion facilitates social inclusion.

AMANDA KHOZA – PANEL MODERATOR

FSCA DEPUTY COMMISSIONERS

KATHERINE GIBSON

ASTRID LUDIN

FARZANA BADAT

What was your initial reaction to being invited to moderate the FSCA Dialogue with the Deputy Commissioners?

I was honoured and excited to be invited to moderate such a meaningful discussion with members of the FSCA's leadership team. As a critical stakeholder, engaging directly on their vision, priorities and expectations for the financial sector. It reflected the FSCA's commitment to being a more responsive, transparent and collaborative regulator.

In a nutshell, what was the discussion about?

I wanted it to be conversational whilst addressing essential issues. The panel focused on the FSCA's strategic priorities for enhancing conduct regulation and building trust in the financial sector. Key topics included:

- Reflections on the FSCA's evolution and achievements over its first five years.
- Upholding ethics, integrity and accountability standards in the industry.
- Adapting to emerging conduct risks around technology, innovation and sustainability.
- Enabling financial inclusion and consumer wellbeing.
- Leadership engagement between the FSCA and industry to drive the right tone and culture.

Why do you think it was an important panel for the sector?

This panel provided a rare public forum for direct, constructive dialogue between senior FSCA executives and the industry. It was an opportunity to clarify the regulator's expectations and philosophy while allowing the industry to share its perspectives. Ultimately, the FSCA and financial institutions have a shared interest in maintaining trust and stability in the sector. Transparent discussions of this nature are critical for finding common ground.

What, in your opinion, were the major takeaways for industry from the session?

- The FSCA is committed to being an agile, integrated, data-driven regulator focused on proactive conduct risk mitigation. The industry should expect continued, albeit collaborative, supervisory intensity.
- Institutions need more work integrating Treating Customers Fairly (TCF) culture, serving vulnerable customers, and responding to emerging digital/cyber and sustainability risks. The FSCA will be looking closely at progress.
- The FSCA and industry collaboration is essential - from engagement on regulatory policy to driving ethical cultures. The industry should proactively step up its partnership with the FSCA.

What were the top four highlights of the conference for you?

- The Governor's keynote and the Commissioner's opening remarks emphasised the interconnectedness of financial stability and market conduct - it set an important tone on shared responsibility.
- The panel addressing greylisting risks showcased strong inter-regulatory coordination on this critical economic issue.
- Discussions on integrating AI and data analytics revealed the immense potential and emerging risks around algorithmic bias and digital exclusion that will require active management.
- The spotlight on sustainability underscored the need for the entire industry to step up on ESG to support South Africa's green transition in a manner that balances environmental and social considerations.

On the imminent COFI bill

“We are not waiting for COFI, I think that is an important point. If you have seen our responsiveness through regulating CASPs, the changing way we are supervising, those are already starting to ‘live’ COFI. We have been doing a lot of work to support the regulatory and supervisory frameworks and we will continue to roll those out, as they are ready. We have established several work groups through our market conduct committee and are actually working with industry to finalise the cross-cutting regulatory frameworks which can be implemented even ahead of COFI, talking to issues like governance and business conduct practices. So, it’s a journey not a destination”

- Katherine Gibson: Deputy Commissioner (FSCA)

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TALKING CULTURE, GOVERNANCE AND ACCOUNTABILITY

In the financial services industry, issues relating to conduct and culture have become increasingly significant due to rapidly changing financial markets, driven by innovation, a shift in consumer expectations and broader societal challenges.

Good conduct is pivotal to strengthening and maintaining public trust and confidence in the financial sector. As culture is unique for various institution, it is important to note that there is no 'good' or 'right' culture, the common denominator for institution comes in asking whether or not their culture is sustainable, healthy, purposeful and safe.

The onus is on financial institutions to embed a culture that consistently promotes sound prudential and conduct outcomes. Entities should question if the culture of their organisations effectively promotes positive outcomes related to the overall safety and soundness of their customers and stakeholders. Reciprocally for regulators, the duty becomes assessing the effectiveness of financial institution's culture in actually delivering on these outcomes.

Financial institutions led by boards that demonstrates an ethical and transparent decision-making culture can help reinforce the implementation of strong governance, risk management and internal control systems. This results in lowered instances of unfair business practices and better outcomes for customers.

LEZANNE BOTHA

SENIOR MANAGER: REGULATORY FRAMEWORK (FSCA)

SINDISWA MAKHUBALO

DEPARTMENTAL HEAD: BANKS AND PAYMENT PROVIDERS SUPERVISION (FSCA)

KEDIBONE DIKOKWE

DIVISIONAL EXECUTIVE: CONDUCT OF BUSINESS SUPERVISION (FSCA)

RIANNE POTGIETER

CHIEF EXECUTIVE OFFICER OF THE COMPLIANCE INSTITUTE SOUTHERN AFRICA

BHEKI MKHIZE

DIVISIONAL HEAD: FINANCIAL CONGLOMERATE SUPERVISION (PA)

"Boards whose decisions are driven solely by interests of short-term-profit-oriented shareholders may set aggressive profitability targets that could incentivise unfair product design, sales and claims handling practices, which could lead to large scale consumer complaints, litigation, reputational damage and significant longer-term losses.

Boards have the responsibility of overseeing effective governance and culture through:

- Overseeing the implementation of desired organisational culture at all levels.
- Streamlining board and governance structures to ensure integrated and holistic prioritisation and oversight of high impact risks.
- Being more robust in their decision making, through better quality tracking of data and management information, and measuring the delivery of key outcomes.
- Assessing diversity and inclusion in the organisations.
- Effective oversight of Senior Management.
- Promoting a culture of openness and debate within the Board, with proper involvement of Senior Management and key persons in control functions.

Institutions are encouraged to ask themselves, is the failure to deliver an outcome rooted in cultural, operational or procedural factors.

COFI will also be instrumental in ensuring an enhanced focus on business principles, culture and governance; and governance arrangements that promote the accountability.

The FSCA and the Prudential Authority are working on a joint standard on Governance requirements for financial institutions. This is a cross cutting standard, which is principles based, focused on good governance outcomes aligned with the King Code.

Once published, the FSCA encourages the industry to engage with the standard and provide input.

"

On the importance of culture

"The importance of culture cannot be overstated. There is a big role for every leader to instil cultural accountability in their spheres of influence. Managing culture is not a once off event. It is something that requires reinforcement."

- Sindiswa Makhubalo - Divisional Executive: Conduct of Business Supervision

RIANNE POTGIETER, CHIEF EXECUTIVE OFFICER OF THE COMPLIANCE INSTITUTE SOUTHERN AFRICA AND ONE OF THE PANELLISTS HAD THIS TO SHARE REGARDING THE CONFERENCE.

The FSCA is a very important stakeholder of the Compliance Institute of South Africa and the compliance community at large. An invitation to participate in the conference was an opportunity to build this relationship, to show our support of the important work that the FSCA does and to add our voice to the broader discussion.

The major takeaways for me from the Culture, Governance and Accountability session included the following:

- The complexity of today's business and financial services environment needs a new regulatory approach. The FSCA's move towards a focus on principles- and outcomes-based regulation ensures that it remains relevant and effective in such a complex environment.
- Collaboration among regulatory bodies and financial institutions will play a crucial role in ensuring that the financial sector continues to evolve in a manner that serves the best interests of consumers and the economy at large.
- Organisational culture is increasingly important in sustaining public trust and confidence in the financial sector. The desired behaviour that puts stability and consumer protection at the heart of what organisations do, can only be effective when driven from within the organisations.
- Compliance professionals will be required to acquire new skills, broaden their knowledge base and follow a strategic, risk-based approach to compliance.

We are all working towards the same goals – just from our specific angles. It was refreshing to hear that, although the mandate of the FSCA is clear, it is an organisation with people who are approachable and open to dialogue.

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SOME KEY TAKEAWAYS FROM THE AI AND CONSUMER PROTECTION DISCUSSION

Artificial intelligence (AI) is the theory and development of computer systems capable of performing tasks that historically required human intelligence, such as recognising speech, making decisions, and identifying patterns. AI is an umbrella term that encompasses a wide variety of technologies, including machine learning, deep learning, and natural language processing (NLP).

The key drivers of AI disrupting the financial services sector include:

- Big data - A wider scope of unstructured data is available: emails, text and voice messages, images and videos are available to offer more personalised services.
- Availability of infrastructure - Cloud technology, high computational resources and infrastructure availability allows for processing of large data at lower costs and efficiency in scalability.
- Regulatory requirements - Automation of data collection processes, improving the speed and quality of decisions and enhancing financial institutions readiness to meet regulatory compliance obligations.
- Competition - AI has become a differentiator: technologies help to harvest data to optimise service offerings, take new offerings to market & provide a more personalised experience to customers.

NOLWAZI HLOPHE

SENIOR FINTECH SPECIALIST
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PHOKENG MOGASE

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(FNB RISK)

South Africans have increasingly taken interest in AI over the last few years, with an increase of 370% over the last year. 60% of South Africans are excited about the possibilities presented by AI.
South African banks have led the way in using AI/ML models they are also the leaders in deploying Gen AI tools that are seeing them use advanced functionality to increase efficiency.
Other segments of the financial services sector are also utilising AI/ML systems, these include insurance and payments due to the rise of fintechs that are using unstructured data.

Financial consumers should be informed about the use of AI techniques in the delivery of a product, when these have an impact on the customer outcome, as well as about machine generated content and any potential interaction with an AI system instead of a human being.

The financial services sector can build on its extensive understanding and experience with existing corporate governance principles to ensure ethical use of AI. Proactive equity assessment of outputs and testing can be used to ensure limited risk of bias and discrimination.

On responsible AI

"When we talk about responsible AI, we are talking about being responsible by design. When we talk about leaders making decisions around AI in terms of what to invest in, we are talking about a sense of intention, and a sense of ownership as well. What we always need to be mindful of is that although AI makes our work easier, we remain in control, we make the decisions, we make the investment, and we define what success looks like."

Ayanda Ngcebetsha - Director: Data and AI (Microsoft South Africa)

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A LITTLE BIT OF A BREAK FROM READING... WATCH SOME OF THE PANEL DISCUSSIONS FROM THE FSCA CONFERENCE BELOW

Sustainable Finance Panel

Watch the Sustainable Finance Panel discussion by clicking on the video

FSCA dialogue on supervisory, regulatory and enforcement plans

Watch the dialogue on supervisory, regulatory and enforcement plans by clicking on the video

Inter-regulatory collaboration under Twin Peaks

Watch the panel discussion on inter-regulatory collaboration under Twin Peaks by clicking on the video

Greylisting panel discussion

Watch the panel discussion on Greylisting by clicking on the video

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REFLECTIONS ON THE GREYLISTING PANEL DISCUSSION, WITH KASHNIE NAIDOO

KASHNIE NAIDOO

CHIEF EXECUTIVE OFFICER & FOUNDER (CRESCENT COMPLIANCE SOLUTIONS)

Meet Kashnie Naidoo, a participant on the greylisting panel. We recently spoke to Kashnie to get her reflections on greylisting and the conference in general.

Tell us a little about you?

I am the founder and CEO of Crescent Compliance Solutions, a bespoke software and compliance consulting company. I am also a Regulatory Specialist for the South African Institute of Stockbrokers. I currently serve on the Board of the Association of Certified Anti-Money Laundering Specialists' (ACAMS) South African Chapter, and most recently have been a judge for the CAMS scholarship Africa which aims to empower talented black financial crime prevention professionals from the African continent.

I am passionate about fostering positive transformation within the South African AML/CFT landscape and effecting meaningful change. I have played an integral role in multiple leadership teams, providing invaluable insights on legislative changes at both the country level and in the financial sector pertaining to Financial Markets and AML.

What are your thoughts on greylisting and efforts taken by the country to address it?

I believe we have made considerable progress in addressing our shortcomings, demonstrating our commitment to the Financial Action Task Force (FATF) through substantial changes to legislation and securing industry buy-in. However, it is equally crucial that we demonstrate the tangible changes and measures implemented at the government level to combat corruption and related issues. This includes not only enacting policies but also ensuring their effective enforcement and transparency. By doing so, we can provide concrete evidence of our dedication to maintaining the highest standards of integrity and accountability, reinforcing our position as a reliable and compliant member of FATF and the international community.

What in your opinion were the major take aways for industry from the session you participated in?

We all need to work together to ensure that we get off the FATF grey list, and achieving this goal requires seamless collaboration between Financial Intelligence Units (FIUs), government entities, supervisory bodies, and accountable institutions. This concerted effort involves not only sharing information and resources but also aligning our strategies and actions towards strengthening our anti-money laundering and counter-terrorism financing frameworks. By fostering a unified approach, we can effectively address the deficiencies identified by the FATF, enhance our regulatory and compliance environments, and restore our credibility on the international stage.

What were the top three highlights of the conference for you?

The theme of building trust was a golden thread throughout the conference, resonating deeply with me. I passionately believe that we can accomplish amazing things together in the industry if we establish trustworthy public-private partnerships that share both strategic and tactical information. By fostering trust, we create a foundation for collaboration, innovation, and mutual support, ultimately enhancing our sector's effectiveness and resilience. These partnerships are crucial for addressing complex challenges and driving sustainable progress, enabling us to achieve our collective goals more efficiently and effectively.

The discussion on AI was extremely illuminating, highlighting not only how AI can accelerate strategies but also how to prepare people in a tangible way for its adoption within the industry. The insights provided shed light on the transformative potential of AI, demonstrating its ability to drive efficiency, innovation, and growth. Furthermore, the conversation underscored the importance of equipping individuals with the necessary skills and knowledge to seamlessly integrate AI into their workflows, ensuring that the workforce is ready to harness the full benefits of this groundbreaking technology.

The conduct, ethics and culture discussion resonated greatly with me, emphasising that conduct must be a business imperative. It highlighted the crucial role of culture as a driver of conduct and demonstrated how an effective culture leads to consistent, conscious behaviours in how institutions manage their products, clients, and overall business operations. By fostering a strong ethical culture, institutions can ensure that their management and board consistently uphold high standards of integrity and responsibility. This, in turn, builds trust with clients and stakeholders, reinforcing the organisation's reputation and long-term success.

What is the importance of collaborating during events such as these, and what value does it add for organisations as well as the public at large?

The importance of collaboration cannot be overstressed. Networking opportunities are invaluable, as meeting and connecting with professionals from various sectors can lead to meaningful relationships, partnerships, and collaborations. Creating an environment where participants can share insights, experiences, and best practices fosters innovation and the development of innovative ideas. Collaborative discussions are instrumental in identifying and solving common challenges, leveraging the diverse perspectives and expertise of all involved.

Kashnie was a participant in the 2019/2020 South Africa FATF county review and subsequently has engaged in the 2023 Vienna FATF Private Session Forum at the United Nations in Vienna. She will also be joining the FATF cohort in Vienna in April of this year.

Greylisting session participants:

FARZANA BADAT

DEPUTY COMMISSIONER (FSCA)

KASHNIE NAIDOO

CHIEF EXECUTIVE OFFICER & FOUNDER (CRESCENT COMPLIANCE SOLUTIONS)

CHARL GEEL

DEPARTMENTAL HEAD: FICA SUPERVISION (FSCA)

PIETER SMIT

ACTING DIRECTOR (FIC)

ISMAIL MOMONIAT

ACTING DIRECTOR GENERAL (NT)

FSCA
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2024

COULD NOT WAIT UNTIL NEXT EDITION...

TERRORIST FINANCING AND TARGETED FINANCIAL SANCTIONS: WHAT ACCOUNTABLE INSTITUTIONS NEED TO KNOW

Terrorists continue finding new ways to raise and move funds around in order to evade safeguards put in place by different countries around the world. By exploiting the vulnerabilities within national anti-money laundering and counter terrorist financing (AML/CFT) frameworks, terrorists and organised crime groups are unfortunately able to weaken the integrity and reliability of financial systems. This results in increased volatility of international capital flows and the undermining of public trust in financial institutions. Consequently, this may also have a dampening effect on foreign direct investments and hamper the growth of national economies as a whole. To curb this phenomenon, it is essential for terrorism-related financial flows and transactions to not only be disrupted but prevented.

This article serves as an important starting point to help accountable institutions learn more about the subject as part of their efforts to prevent terrorist financing risks from materialising.

What is terrorist financing?

Terrorist financing is described by the Financial Intelligence Centre (FIC) as the collection or provision of funds for the purpose of enhancing the ability of an entity or anyone who is involved in terrorism or related activities to commit a terrorist act. Funds may be raised from legitimate sources, such as personal donations and profits from businesses and charitable organisations, as well as from criminal sources, such as the drug trade, the smuggling of weapons and other goods, fraud, kidnapping and extortion.

What do we mean by "terrorist financing risk"?

Terrorist financing risk (TFR) refers to the probability that funds or assets intended for a terrorist organisation are raised, moved, stored, or used in or through a jurisdiction, whether legitimate or illegitimate.

Assets or funds that are owned or controlled by individuals or groups involved in terrorist activities are referred to as **Terrorist property (TP)**.

These assets can be used to finance terrorist acts and are subject to seizure and forfeiture by law enforcement agencies. These assets or funds are accounted for in the **Terrorist property report (TPR)**, which must be submitted by an accountable institution in terms of section 28A of the Financial Intelligence Centre Act, No. 38 of 2001 (FIC Act). This requires the accountable institution to scrutinise information about clients with whom they have business relationships to determine if any of these clients are individuals or entities mentioned in the notice given by the Director about the adoption of a resolution by the United Nations Security Council, providing for financial sanctions which entail the identification of persons /entities against whom member states must take actions specified in the resolution.

The accountable institution must submit a report to the FIC, based on their knowledge of the property under their control. An objective test is used. This is done to help authorities track and prevent the illegal funding of terrorist organisations, ultimately contributing to national security efforts to combat terrorism.

South Africa's Terrorism Financing National Risk Assessment

With the above concepts in mind, it is beneficial to now understand the national risk assessment on terrorism financing, which assists a country in identifying, assessing and understanding its TF risks so that appropriate CFT measures can be applied commensurate to the level of risk identified. This leads to stronger and more credible national CFT strategies, assists in the effective implementation of a risk-based approach (RBA) towards CFT measures and ultimately contributes towards the dismantling and disrupting of terrorist networks in a country.

To facilitate greater awareness and understanding of the nature of TFR that exist in South Africa, the country recently completed its second Terror Financing National Risk Assessment (TF NRA 2024). The TF NRA 2024 describes the threats, vulnerabilities and possible impact of TF on South Africa's safety and stability as well as neighbouring countries. It is meant to assist, among others, accountable institutions to identify risks and develop appropriate responses to reduce such risks by improving prevention, monitoring and enforcement mechanisms.

Based on the results of the TF NRA 2024, South Africa's TF threat and risk profile increased from *moderate* (2014-2018) to *high* (2019-2024). It was established that South Africa is a hub, and may be specifically targeted, for terrorist fund-raising, storage, and transfer through criminal exploitation of formal, informal, illicit, and alternative economies.

South Africa's TF vulnerabilities relate to the characteristics of specific sectors, the country's unique geographical position and sophisticated financial system making it attractive for terrorists and their enablers. These vulnerabilities include the financial products or services that render them susceptible to TF, as well as the use of electronic and online platforms to raise, store, move, and access funds and assets for terrorism purposes, including crypto assets.

It is crucial for accountable institutions and South Africans at large to be alert about the prevalence of TF risks, and to identify and report on suspected TF activities in order to protect the country and the financial system.

The public version TF NRA 2024 may be accessed on the FIC's website by clicking here.

What are Targeted Financial Sanctions?

South Africa is a member of the Financial Action Task Force (FATF), which requires countries to implement targeted financial sanctions (TFS) to comply with the United Nations Security Council Resolutions (UNSCRs) relating to the prevention, suppression, and disruption of proliferation of weapons of mass destructions (WMD) and its financing.

The consolidated TFS List includes designated individuals and entities that are terrorists or terrorist financiers, subjected to sanctions imposed by the UNSC.

FATF Recommendations 6 and 7 require countries to implement TFS regimes to comply with the UNSCRs.

In the context of South Africa, the FIC Act requires accountable institutions to comply with their obligations related to TFS, in particular the obligation to screen clients, identify positive matches, freeze assets without delay and file the necessary reports with the FIC as soon as possible.

Obligations of accountable institutions

Accountable institutions are required to comply with sections 21, 26B, 28A and 29 of the FIC Act read with section 26A, Guidance Notes 6A and 7, as well as PCC 44A.

These require accountable institutions to:

- Scrutinise clients against the TFS list. If there is a positive match on the TFS list, the accountable institution must "freeze and report", and the client **must not be onboarded**. This means that the accountable institution must immediately cease any activity, which can include not releasing any property to the designated person or entity or persons acting on behalf of the designated person or entity.
- Report TPR to the FIC regardless of whether a transaction is concluded or not.
- Report to the FIC if any of the following circumstances exist:
  - The business has received or is about to receive property which is connected to terrorism and related activities;
  - A transaction or series of transactions to which the business is a party to facilitate or is likely to facilitate the transfer of property which is connected to an offence relating to the financing of terrorist and related activities; or
  - Prohibitions relating to persons and entities identified by the UNSC under section 26B of the FIC Act.
- Ensure adequate record keeping of compliance with these obligations. This is important as compliance with these requirements **must be demonstrated** by accountable institutions and this will be assessed when supervisory bodies, including the Financial Sector Conduct Authority (FSCA) undertakes its AML/CFT supervisory activities.
- Risk rate the products, distribution channel, client type and geographic location used for the financing of terrorism or proliferation financing as high risk in the accountable institution's business risk assessment. This should result in enhanced customer due diligence for business relationships which are identified as high risk for the financing of terrorism or proliferation financing.

Available guidance for accountable institutions

In order to provide guidance to accountable institutions, the FIC issued Guidance Note 6A on Terrorist Financing and Terrorist Property Reporting Obligations in terms of Section 28A of the FIC Act and Public Compliance Communication 44A (PCC 44A), on the implementation of TFS in South Africa.

Furthermore, the FIC provides Guidance Note 4B on reporting suspicious and unusual transactions and activities to accountable institutions.

PCC 44A provides that accountable institutions' Risk Management and Compliance Programmes (RMCPs) **must** make provision for the manner in, and processes by, which they will:

- scrutinise client's information;
- freeze designated persons and entities' property **without delay**; and
- report to the FIC **as soon as possible**.

The TFS list can be accessed on the FIC's website via the online search tool. The tool assists accountable institutions in identifying potential matches between their clients' names and/or entity names on the UNSCR list.

Accountable institutions can also make use of other automated systems that use a third-party service provider(s) to access the TFS list. The accountable institution remains responsible for complying with its obligation to scrutinise clients, by making sure that the screening lists are accurate and up-to-date and that the results are true.

The FSCA urges accountable institutions to consider TF NRA 2024 as they develop, maintain, and implement their RMCPs and to help deepen their understanding of TF risks. This is vital to ensure that they implement appropriate controls to mitigate the risk of their businesses being exploited by terrorists, terrorist financiers or those involved in terrorist-related activities.

In order to foster awareness about TF, the FSCA has recorded an in-depth webinar on the TF NRA, which is available on the FSCA YouTube channel. Accountable institutions and other interested stakeholders are encouraged to view the webinar and comment on it.

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Financial Sector
Conduct Authority