



Legal Services

FINANCIAL SERVICES



## ON THE SCALES 14 OF 2018

### Guidance Note 2 of 2018 – Clarification on Directive 8 Prohibition on the Acceptance of Gratification

Earlier this year, the then Financial Services Board ('FSB') issued Directive 8 called "Prohibition on the Acceptance of Gratification" (please see *On the Scales 9 of 2018*). It set out that officials of, and service providers to, a fund must not be involved in any conduct constituting bribery, fraud or corruption, and any such involvement will have a bearing on such person's fitness and propriety to hold office. The Directive defines what constitutes 'gratification' and those defined types of gratification may not be accepted by fund officials, unless the regulator agrees in advance they can be accepted.

The FSCA has received many queries about Directive 8. The FSCA has released Guidance Note 2 to provide practical guidance on the application of Directive 8.

If there is any inconsistency between Directive 8 and Guidance Note 2, then Directive 8 will apply.

## Summary

- Directive 8 was issued earlier this year dealing with the Prohibition on the Acceptance of Gratification.
- The FSCA has received queries about the interpretation of Directive 8.
- The FSCA has released Guidance Note 2 to clarify the practical application of Directive 8.
- Reporting of breaches or potential breaches of Directive 8 must be made to the FSCA.
- Directive 8 is not intended to stop legitimate training provided by service providers for fund officials, but preferably funds must pay the costs for training, travel and accommodation.
- Service providers may pay for business-related meals, provided the meals are legitimately for the purpose of conducting the business of the fund.
- Fund officers may not accept invitations to entertainment events paid for by service providers.
- Token gifts may be accepted by a trustee, subject to an annual limit of R500 per service provider.
- If it is necessary for a fund officer to conduct a due diligence or other fund-related activity, then all costs (including travel and accommodation) must be paid by the fund.
- If a trustee or a principal officer has an interest in a service provider to the fund, this would be a breach of Directive 8 and a conflict of interest, unless the fund cannot reasonably appoint any other service provider.
- If there is any uncertainty about whether a practice complies with Directive 8 or not, then the FSCA urges funds to avoid that practice.

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### Reporting any non-compliance with Directive 8

All service providers and fund officials have a duty to report any actual or potential breach of Directive 8. Failure to make such a report is a breach itself of Directive 8.

Reporting to the FSCA must be done immediately upon becoming aware of a breach or potential breach.

The report must preferably be submitted in writing. Information Circular 1 of 2018 provides guidance on making reports and disclosures (see On the Scales 3 of 2018).

### Training

Directive 8 is not intended to limit or stop legitimate training provided by service providers to fund officers.

The FSCA prefers that funds pay the cost of training, travel and accommodation. If the training is free, then the fund should pay for the travel and accommodation costs.

If a service provider provides training at no cost, which includes refreshments, then such training must be open for registration to the general public or a general category of persons.

The actual cost of training, whether paid for by the fund or offered free by the service provider, must still be reasonably justifiable.

### **Business-related meals and similar considerations**

Service providers may pay for business-related meals, provided the meals are legitimately for the purpose of conducting the business of the fund.

The activities must be kept to the minimum necessary to maintain effective business relationships and should not be exorbitant.

The value of any meals paid for by a service provider must be declared in the fund's gift register.

### **Entertainment**

Fund officers may not accept invitations to events paid for by service providers.

These prohibited events include hunting, sporting events, meals, coffee, concerts and jazz festivals. Service providers are cautioned not to justify an entertainment event in an attempt to legitimise that event as being not contrary to Directive 8.

Retirement fund officers must apply their minds to whether an invitation is for a legitimate purpose or simply for entertainment.

*Comment: our interpretation of this is that a meal that forms part of a legitimate business activity is permitted. For example refreshments provided at a trustee meeting or training is acceptable. However a meal that is purely for entertainment purposes and is not linked to fund activities or business is not permitted.*

### **Token gifts**

Token gifts can include pens, calendars, mugs and chocolates.

Token gifts may be accepted by a trustee, subject to an annual limit of R500 per service provider.

The FSCA purpose behind this limit is to prevent a goodwill concession being converted into corrupt activities.

*Comment: our interpretation is that the R500 annual limit applies per trustee, per service provider.*

### **Due diligences and other fund-related activities**

If it is necessary for a fund official to conduct a due diligence or other fund-related activity, then all costs (including travel and accommodation) must be paid by the fund.

The due diligence or other activity should not be an excuse to go on holiday at the expense of the fund.

There must be a proper motivation for such activity, including considering the number of fund officers required to go and whether those going have the right skill and experience to conduct the due diligence or fund-related activity.

After any due diligence or activity has been concluded, the fund officer must produce a written report to the board.

### **Sponsored funds**

Sponsor-appointed trustees can be remunerated by the sponsor of the fund.

This applies to section 26(2) trustees as well.

*Comment: often in the case of closing funds there are insufficient assets to pay a section 26(2) trustee and so the sponsor remunerates the section 26(2) trustee.*

### **Gratification which objectively viewed creates a conflict of interest**

As far as possible, a fund should pay its own costs, unless circumstances dictate otherwise and no conflict of interest is created.

Administrators can pay the closing costs for shell or dormant funds, without breaching Directive 8.

In an underwritten fund, the administrator can meet fund expenses without this being a conflict of interest. Trustees must still exercise their minds independently.

If a trustee or a principal officer has an interest in a service provider to the fund, this would be a breach of Directive 8 and a conflict of interest, unless the fund cannot reasonably appoint any other service provider. An example given is of a trustee or principal officer that is also an employee or director of a law firm that is appointed by the fund to provide legal advice.

If there is any uncertainty about whether a practice complies with Directive 8 or not, then the FSCA urges funds to avoid that practice.

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*If you need more information, please contact your consultant.*

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