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(To all self-administered pension funds)

PERSONAL ACCOUNT TRADING : FSB POSITION PAPER AND GUIDELINES

After thorough research it was decided to issue papers on Personal Account Trading and Guidelines for Personal Account ("PA") Trading Rules for Employees of Participants in the Financial Markets.

These guidelines are the result of a co-operative effort between the Banking Supervision Department of the South African Reserve Bank and the FSB, involving a thorough research of the subject. The Reserve Bank issued a similar circular in terms of the Banks Act. This is, therefore, a consolidated regulatory effort.

I thank you for your co-operation in this regard.

REGISTRAR OF PENSION FUNDS

Enclosures

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PERSONAL ACCOUNT TRADING POSITION PAPER

1. Introduction

The purpose of this paper is to set out the position of the Financial Services Board (FSB) on personal account trading ("PA trading") by employees of financial institutions. PA trading encompasses individual employees of a financial institution trading in securities or other financial instruments, the risks and rewards of which are for their own personal direct or indirect benefit.

The FSB is of the opinion that in the final analysis the only way to avoid the problems arising from PA trading is for financial institutions to prohibit employees from engaging therein. It is however recognised that financial institutions could experience difficulty in employing sufficiently competent staff if such a prohibition is applied.

If PA trading is permitted, it is imperative that certain internal control procedures be applied. The management of the financial institution will consequently have to accept responsibility for the establishment of the necessary systems and controls in order to prevent

- Conflicts of interest,
- Prejudice towards clients, and
- Prejudice towards the financial institution itself

2. Underlying Principles

The underlying principles of this approach are

- ❑ Any standard or code should help to promote the regulatory objectives of stability, efficiency and investor protection,
- ❑ Only independent, duly authorised, fit and proper people should manage and supervise employees who are active in PA trading,
- ❑ Stringent risk management should underlie all decisions of those managing and supervising the PA trading of employees, and
- ❑ Contamination between risks arising from normal trading activities and those arising from PA trading activities should be minimised

3. Role of the FSB

With regard to PA trading, the aim of the FSB is to ensure the efficiency and stability of the financial system and of individual financial institutions. In addition the introduction of adequate investor protection mechanisms will be achieved through the implementation of

- ❑ Sound corporate governance, and
- ❑ Comprehensive systems of internal control

In order to achieve these aims, the FSB will facilitate the establishment of acceptable standards. Financial institutions are expected to establish their own set of controls and rules. In order to assist with the development of acceptable standards the FSB has formulated the attached guidelines.

These guidelines should not be seen as being comprehensive in all situations. Furthermore, it will be necessary to apply more stringent rules to staff who are directly involved in certain functions (such as dealers and portfolio managers).

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GUIDELINES FOR PERSONAL ACCOUNT ("PA") TRADING RULES FOR EMPLOYEES OF PARTICIPANTS IN THE FINANCIAL MARKETS

A financial institution is expected to establish its own set of rules governing PA trading. From the point of view of the Financial Services Board (FSB), these rules shall as a minimum, include the following

1. **Dedicated Personnel**

A financial institution should have adequate resources and dedicated and appropriately empowered senior staff responsible for

- ☐ Approval of all PA trades in financial instruments,
- ☐ Keeping of proper records of all such transactions,
- ☐ Reporting to the compliance officer, audit committee, and the board of directors,
- ☐ Reporting any material transgressions to the appropriate regulator, and
- ☐ Closing positions entered into in contravention of the rules

2. **Prior Written Approval**

All employees of a financial institution must be required to obtain written approval before entering into any transaction (including for a connected person). The written approval must have an expiry or review date. The employee will have to declare the following

- ☐ The intent of the PA transaction, stating whether the transaction is for speculative or for investment purposes,

- The type of security,
- The nature of the transaction (i.e. Purchase or sale, quantity, and proposed date and time, etc),
- The broking firm through which the transaction will be executed (Off-market trades in listed securities should be prohibited), and
- The identity of the counterparty for unlisted securities

In terms of dealing staff, it is highly recommended that they be obliged to hold their positions for a minimum period of 30 days

3. Conditions of Employment

It is imperative that the rules governing PA trading should form part of the conditions of employment

4. Conflict of Interests

The trader should trade PA securities through the appropriate trading desk of his own financial institution or through an appointed, recognised and approved third party. The rules must ensure that conflict of interests between the employee and clients are prevented. This is particularly relevant in a situation where the employee is acting as a discretionary portfolio manager. As a general rule the trader or portfolio manager should not be allowed to conduct PA trading in the same counter he or she is trading for clients or his employer within a set period of such client or proprietary trades without specific prior approval. This specific approval must be from the compliance officer and senior dealer to ensure that all relevant client and proprietary trades have been concluded prior to his or her PA trading in that counter. Employees may not request or accept any credit or special dealing facilities with external parties

5. New Listings

The rules must be applied equally to new listings

6. Application of Rules

The rules must be applied to all employees, including senior management, and appropriate disciplinary action provided for

7. Underwriting

The employee may not act as an underwriter or sub-underwriter of securities if the financial institution is acting in that capacity, or if the employee knows that the financial institution will be offered a participation, underwriting or sub-underwriting in that security

8. Future Developments

These guidelines are to a large extent based on practitioner input, which should ensure a market-supported solution. It is therefore hoped that these guidelines will make an important contribution to the development of minimum standards governing PA trading in securities in South Africa. There is also a need to update and make changes when deemed appropriate in order to maintain the integrity and stay abreast of international developments

GLOSSARY

Connected person means:

- (i) A spouse or partner,
- (ii) Minor children,
- (iii) Any person in a business or profit sharing relationship with the employee, including partners in an investment club,
- (iv) A trust in which the employee or any person mentioned in (i) or (ii) is a beneficiary,
- (v) A company in which the employee or any person mentioned in (i), (ii) or (iv) is a shareholder,
- (vi) A pension fund (other than a pension fund managed by the institution) of which the employee or any person mentioned in (i), (ii) and (iii) is a beneficiary, and
- (vii) Or any other accounts where the person has a direct or indirect benefit

Employee means:

- ☐ Any person employed by the institution
- ☐ Including persons dealing on behalf of the institution or its clients,
- ☐ Any person who is privy to confidential or proprietary information which could result in a conflict of interest if the employee used the information to his/her advantage, and
- ☐ Includes a person on secondment or contract, and connected persons

Rules means:

The personal account trading rules enforced by the institution from time to time and which comply with the minimum standard set out in this document

Securities means:

Includes "securities and financial instruments" as defined in the Financial Markets Control Act, (Act 55 of 1989), the Stock Exchanges Control Act (Act 1 of 1985) respectively, and any unlisted instruments such as bonds, futures, options, forward rate agreements, swaps, equities and derivatives of any of these, but excludes all unit trusts other than unit trusts listed on a recognised exchange or with assets under management by the institution

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