STATEMENT SUPPORTING DRAFT PRUDENTIAL STANDARD – REGULATION 28 QUARTERLY REPORTING REQUIREMENTS FOR PENSION FUNDS

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FSCA
Financial Sector
Conduct Authority

1 PURPOSE OF THE STATEMENT

1.1 This Statement relates to the draft Prudential Standard – Regulation 28 Quarterly Reporting Requirements for Pension funds ("draft Prudential Standard"), proposed to be made by the Financial Sector Conduct Authority ("FSCA") in terms of regulation 28(8)(a) of the Regulations under the Pension Fund Act, 1956 (Act No. 24 of 1956), published in Government Notice R98 of Government *Gazette* No. 126 on 26 January 1962, as amended from time to time ("Regulations"), read with section 105 and 292(2)(b),(3) and (4) of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) ("FSR Act").

1.2 This Statement is published in accordance with section 100(1) of the FSR Act and is intended to support and give context to the draft Prudential Standard that is published for public comment. The main purpose of this Statement is to explain the need for, the expected impact of, and the intended operation of the draft Prudential Standard and to explain the reasons why the delay involved in complying with sections 98 and 99 is considered likely to lead to prejudice to financial customers or defeat the object of the proposed regulatory instrument.

2 STATEMENT OF NEED AND THE REASONS FOR URGENCY - POLICY CONTEXT AND PROBLEM DEFINITION

2.1 Regulation 28 protects retirement fund member savings by limiting the extent to which funds may invest in a particular asset or in particular asset classes. Regulation 28(8)(a) provides that the FSCA, *"… may prescribe the format, content and any other particulars in respect of disclosure of compliance with this Regulation".* The disclosure reports are referred to as 'quarterly reports' and are currently prescribed in different Notices.

2.2 Regulation 28 was revised in July 2022 and, among others, requires additional reporting requirements in relation to infrastructure assets and other amendments to the asset spreading requirements. The Regulation 28 amendments come into effect on 3 January 2023. It is imperative that the quarterly reports take into account the amendments and ensure that pension funds appropriately report on these matters.

2.3 Section 98 of the FSR Act requires that the maker of a regulatory instrument must publish a draft of the regulatory instrument, together with specified documents, for a period of at least six weeks. In addition, section 103(1) of the FSR Act requires that a maker of a regulatory instrument must submit the regulatory instrument to Parliament, for a period of at least 30 days while Parliament is in session.

2.4 However, section 100 of the FSR Act provides that if the maker of a regulatory instrument determines that compliance with section 98 is likely to lead to prejudice to financial customers or harm to the financial system, or defeat the object of the proposed regulatory instrument, the maker must, before making the instrument –

- publish a draft of the regulatory instrument, together with specified documents, for a period of at least seven days; and
- submit the regulatory instrument, together with specified documents, to Parliament in terms of section 103(2) of the FSR Act. Section 103(2) provides that before making a regulatory instrument in terms of section 100, the maker of the regulatory instrument must submit to Parliament, whether in session or not, the documents mentioned in section 100(1) (a) for a period of at least seven days (which period may run concurrently with the seven days referred to in section 100(2)).

2.5 The effective date, i.e. 3 January 2023, of the amendments to Regulation 28 necessitate urgent amendments to the quarterly reports. For this reason, the FSCA intends to issue this Prudential Standard as an urgent instrument as contemplated in section 100 of the FSR Act. The FSCA is of the view that should the process prescribed in sections 98 and 103(1) be adopted when amending the quarterly reports, it will significantly delay the finalisation of funds' quarterly reports.

2.6 A delay in the implementation of the new quarterly reports may defeat its purpose, which is, among other things, to give clear and timely direction to funds on how they should report. The urgent publication of the new quarterly reports will promote legal certainty by ensuring that pension funds know exactly which information is required and in what format the information must be submitted to the FSCA, immediately after the amendments to Regulation 28 take effect. This will enable pension funds to timeously update their systems and reporting processes in accordance with the requirements set out in the new quarterly reports.

2.7 In addition, if the normal process is adopted (which will result in a delay in obtaining information) the FSCA will have to implement an alternative measure[1] to obtain the information contemplated in these new reports, whilst simultaneously following the process prescribed in sections 98 and 103(1) to amend the current quarterly reports, pension funds will have to incur costs to either–

(a) update their systems and reporting processes to enable them to provide the requested information; or

(b) use resources to provide the information manually, pending finalisation of the format of the quarterly reports.

2.8 Should an alternative measure be implemented (as referred to in paragraph 2.7) pending the finalisation of the Prudential Standard, and the draft quarterly returns change as a result of the consultation process, pension funds will have to update their systems and reporting requirements again in order to conform to the changed requirements or format, resulting in additional costs. Delaying the implementation of the new quarterly reports may therefore result in greater costs being incurred by pension funds.

2.9 Accordingly, by following the procedure in section 100, which includes consultation, and putting in place final requirements, it will, as referred to above, promote legal certainty and avoid additional costs being incurred by the fund, which will likely negatively affect the benefits of pension fund members.

2.10 In addition, the new quarterly reports will not only enable funds to report effectively, but to identify any non-compliances, or potential non-compliances, timeously. Should the implementation of these new quarterly reports be delayed, and possible non-compliance not identified, it is likely to lead to prejudice to financial customers, placing pension fund members at risk, and could also result in harm to the financial system.

2.11 Therefore, a need exists to urgently update the quarterly reports for pension funds in line with the recent amendments to Regulation 28, to ensure disclosures, consistency and transparency in the application of reporting requirements across all pension funds, to promote legal certainty and to protect pension funds, and members of those funds, against the incurrence of additional costs.

3 SUMMARY OF THE DRAFT PRUDENTIAL STANDARD

3.1 The draft Prudential Standard prescribes quarterly reports for pension funds and also incorporates a revised and updated quarterly reporting format. In addition, the draft Prudential Standard provides enhanced details, and the specific paragraphs of the quarterly reports are expanded on in line with recent amendments to Regulation 28.

[1] E.g. through a request for information under section 131 of the FSR Act.

3.2 The draft Prudential Standard now also includes quarterly reporting in respect of Infrastructure, overall limit for Infrastructure across all classes and overall limit for all instruments per entity or issuer. Non-compliance or breaches in terms of sub-Regulation 3 of Regulation 28 at fund and member level must also be reported (where applicable) along with the asset allocations at fund level. Reporting in respect of Infrastructure Assets list issuers or entities which exceeds 5% of total assets must also be reported. Matters related to environmental, social and governance issues must be reported. Some of the other changes include the splitting of the hedge funds and private equity asset allocations and the revised housing loans and private equity limit.

3.3 The draft Prudential Standard also replaces the following Notices:
(1) Notice No. 2 of 10 June 2011;
(2) Notice No. 3 of 19 December 2011;
(3) Notice No. 3 of 31 May 2012; and
(4) Notice No. 6 of 2 October 2012.

4 STATEMENT OF IMPACT OF THE PRUDENTIAL STANDARD

4.1 The Prudential Standard will have an immediate financial impact on all funds as there are additional areas of reporting required. Therefore, all funds need to have additional resources to ensure accurate reporting. However, it is submitted that the impact is mainly as a result of the changes to Regulation 28, and not as a direct result of this Prudential Standard. The Prudential Standard is merely a tool to facilitate reporting of compliance with Regulation 28, including the new changes. No significant financial impact is envisaged in respect of funds that were not required to submit these reports previously.

4.2 Therefore, the Authority does not expect a major financial impact on funds because of this Prudential Standard. The impact on all funds to report their asset allocations will mostly be manageable however it’s imperative for all funds to make a provision for additional reporting required.

4.3 The new reports will allow funds to detect non-compliance with Regulation 28 earlier and take proactive remedial action. In addition, these compulsory Regulation 28 quarterly reports will assist all funds when preparing their annual financial statements.

5 STATEMENT OF INTENDED OPERATION OF THE PRUDENTIAL STANDARD

5.1 The draft Prudential Standard is consistent with the objects of the FSR Act and PFA, and specifically the mandate of the FSCA.[2]

5.2 The draft Prudential Standard will become effective on the date of publication.

5.3 Following the implementation of the Prudential Standard, the Authority will assess and evaluate the effect of the Prudential Standard on a continuous basis as part of its regulatory and supervisory responsibilities.

[2] As exercised in terms of section 292(2)(b), (3) and (4) of the FSR Act.