FINANCIAL SERVICES BOARD

FINANCIAL ADVISORY AND INTERMEDIARY SERVICES ACT, 2002 (“FAIS ACT”)

FAIS CIRCULAR 11/2012
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Circular on Financial Services Providers who operate Cash Management System Accounts

1. Introduction

There is a growing number of Financial Services Providers (“FSPs”) rendering financial services on the Cash Management System (“CMS”) bank account currently offered predominantly by Investec Bank – Corporate Cash Management Account (“CCM”) and Nedbank – Corporate Saver System Account (“CSS”).

There is some confusion in the industry as to whether a section 19(3) audit report is required from FSPs who operate a CMS account or not. To clarify this issue and state the Registrar’s position, it was deemed necessary to clarify the matter herewith.

2. What is the CMS Account?

The CMS Account is an online banking administration system offered by banks to various types of businesses.

3. How the CMS account operates?

The CMS Account is similar to a trust account maintained by professionals for the purpose of holding money on behalf of third parties “on account” for a specified purpose. The account is used by corporate entities and persons to accelerate the collection of deposits, facilitate investments, manage cash efficiently and control payments to trade creditors. The account usually combines a money market fund from which interest is paid and a brokerage or investment account.
The CMS account is an online banking administration system and is currently offered by banks to the following types of businesses:

- Attorneys.
- Estate Agents.
- Accountants and Auditors.
- Independent Financial Advisors.
- Investment Managers.

The above-mentioned entities or persons are referred to as agents in the banking industry. Therefore, in order for the agents to access the online banking administration systems they are required to enter into a written agency agreement with the bank, in terms of which the agent is authorised by the bank to perform the following activities on behalf of the agents’ clients:

- Open a bank account.
- Transact.
- Negotiate interest rate with the bank on behalf of the agent’s clients.
- Perform inter-bank transfers (electronic fund transfers).

In addition the bank performs due diligence on the business of each agent. The due diligence process entails the following:

- Independent Financial Advisors, Investment Managers and Accountants must be licensed as Financial Services Providers.

- Attorneys and Estate Agents must provide proof that clients’ monies that will be invested in the CMS account are regulated as trust monies in terms of the relevant enabling legislation.

After signing the agency agreement with the bank, the agent will market the CMS account to their clients. Clients agreeing to invest money into the CMS account will earn interest negotiated between the agent and the bank. The interest offered by the bank to the clients of the agent is determined by the total size of the agent’s client base. This means that agents with a large client base could negotiate a higher interest for their clients. It should also be noted that if the rate of interest negotiated between the bank and the agent is for example 5%, all clients of the agents will earn 5% interest on their funds in the CMS account irrespective of the amount of money invested. Interest earned on these accounts is usually higher than interest earned on other bank accounts.

4. The structure of the CMS account

The CMS account can be opened in the following two ways:

4.1 Segregated accounts

In this case, an account is opened and registered in the name of the client. Clients who wish to invest their money into the CMS account are required to
sign an agreement (referred to as power of attorney) with their agent authorising the agent to perform the following activities:

- Open a CMS account on behalf of the client;
- Transact on this account on behalf of the client;
- Perform inter-bank transfers (electronic fund transfers); and
- Report to the client the interest earned on this investment.

The agreement signed between the client and the agent is not approved or vetted by the banks. A perusal of some of the agents’ agreements sighted by this Office shows that the agent only transacts on the CMS account on the client’s direct instruction, whereas other agreements stipulate that the agent will have full discretion when transacting on these accounts.

After the agent and its clients have signed and agreed to the terms and conditions of the agreement, the agent opens the CMS account in the client’s name and each client is allocated a bank account number. Each segregated account is linked to an agent through an agent reference number which is similar to a broker code. The agent then signs a power of attorney with the client in terms of which the agent will have certain powers over the segregated account.

The following are the different types of CMS accounts that can be linked to the main CMS account:

- 32 day notice - funds available on notice.
- Term deposits - from as little as one day.
- 1-12 months fixed deposits.

Depending on the wording of the signed agreement between the client and agent, the agent may perform the following activity:

- Transfer client’s investment from the main CMS account to any of the sub accounts mentioned above on the client’s instruction.

4.2 Umbrella account

In certain cases, an account is opened and registered in the name of the agent. Agents who are mainly investment managers, operate the CMS account in an umbrella format. Rather than opening separate accounts and allocating separate account numbers for each client, the agent opens one account similar to a trust account in the agent’s name but designated as a client funds account. All clients’ funds are invested in this one account and the funds are distinguished through sub-accounts allocated to each client of the agent. Agents operating the CMS account in this manner are deemed to be handling or holding clients’ funds and the requirements of Section 19 (3) of the FAIS Act must be complied with.

5. Implication of the CMS account on the requirements of FAIS Act

5.1 Authorisation in terms of section 7 of the FAIS Act
Any person operating the CMS account is rendering financial services to a client with regard to bank deposits. These deposits can be:

- Deposits as defined in the Bank Act- exceeding 12 months; and/or
- Deposits as defined in the Bank Act- 12 months or less.

The type of license (Category I or Category II) to be applied for and acquired will depend on the type of service and agreement between the agent and the client. There is a strong indication that there may be persons or entities who operate a CMS account but are not licensed in terms of the FAIS Act. It is a requirement that every person or entity which renders a financial service through a CMS Account which equates to deposits as defined in the FAIS Act should be licensed as Category I or II FSP.

5.2 Submission of Section 19(3) report

Section 19(3) of the FAIS Act read with Section 10(1)(d) of the General Code of Conduct requires FSPs who hold client funds to –

- Open a separate account to be used for holding client funds.
- Account for such client funds separately.
- The separate account used for holding client funds should be audited and a report of such an audit should be submitted to this Office.

After considering the structure and operations of a CMS account, it would appear that not all agents who operate this type of account would be required to submit a section 19(3) report. The following recommendations are proposed:

- Agents operating segregated CMS accounts and only transacting on client’s instruction, must be licensed as Category I FSPs and the section 19(3) requirement is not applicable.
- Agents operating segregated CMS accounts and using full discretion to operate this account and carry out transactions on it must be licensed as Category II FSPs and the section 19(3) requirement is not applicable.
- Agents operating Umbrella CMS accounts and only transacting on client’s instruction must be licensed as Category I FSPs and the section 19(3) requirements is applicable.
- Agents operating Umbrella CMS accounts and given full discretion to operate this account and transact on it must be licensed as Category II FSPs and the section 19(3) requirement is applicable.