BMF SUBMISSION ON TRANSFORMATION OF THE FINANCIAL SERVICES SECTOR

10 MARCH 2017

BACKGROUND

The Black Management Forum (BMF) is a non-racial, thought leadership Organisation with the main purpose of influencing socio-economic transformation of our country, in pursuit of socio-economic justice, fairness and equity.

The organisation stands for the development and empowerment of managerial leadership primarily amongst black people within organisations and the creation of managerial structures and processes, which reflect the demographics and values of the wider society.

It is against this background that the BMF spearheads the process of systemic transformation of the workplace anchored largely through the Employment Equity Act of 1998 (EE Act) and Broad-Based Black Economic Empowerment Act of 2003 (BBBEE Act) as amended.

SCOPE AND NATURE OF THE SUBMISSION

The BMF submission is confined to ***broad policy principles*** against which we express our **grievances** with the Sector. We thought it served no purpose to deal with detailed technical shortcomings of various pieces of regulations and/or Acts for reasons espoused hereunder. Nonetheless, the core of our submission is as follows.

KEY AND STRUCTURAL TRANSFORMATION ISSUES IN THE SECTOR

1. Existence of Sector Codes in general and the Financial Sector Code (FSC) in particular.

The BMF is opposed to the FSC as a matter of principle:

A. Though B-BBEE Act does provide for Sector Codes, the over-arching and harmonising nature of the BBBEE Generic Codes as contained the Broad Based Black Economic Act (BBBEE) renders sector specific Codes unnecessary and as a hindrance to transformation especially where the sector specific Codes have lower minimum targets than what is prescribed in the Generic Codes.

B. Sector Codes in general and the FSC in particular are minimalist by design, they tinker rather than being fundamentally transformational. For example, the Draft FSC Code has a 10% target for direct ownership which is 15% below a 25% target set in the BBBEE Generic Codes.

C. The FSC seeks to buttress current non-compliance culture by providing new B-BBEE labels. This characteristic explains the popularity of the Sector Codes within what is an intransigent sector, the Financial Services Sector.

D. The BMF submits strongly that even in light of the very weak Sector Codes, the Financial Services Sector continues to fail to meet its own targets and thus we reject the FSC as dubious at best and a red-herring at worst.

RECOMMENDATION: The Standing Committee must engage with the DTI and argue that if the FSC is to remain, it must be amended to meet or exceed the minimum requirements set by the BBBEE Generic Codes.

2. Access (To Finance) and Empowerment Financing

As a matter of principle, the BMF is opposed to these so-called 'industry specific' elements contained in the FSCC.

A. The BMF objects to access and empowerment finance as a part of the areas against which to measure the Financial Services Sector on transformation, providing banking services and lending money and/or asset financing is in the normal course of business for financial institutions. These measures are at odds with the permissible "deviation" grounds as contained in the Statement 003 of the Code of Good Practice.

RECOMMENDATION: The Standing Committee must engage with the DTI and strongly recommend that Empowerment Financing be removed altogether.

3. Once Empowered, Always Empowered principle.

A. We are of the view that this needs to be scrapped all together. This is too general and almost goes against normal business principles. Lack of sustainability lies behind the high failure rate of start up's in the country. We need a comprehensive approach to ensure that businesses operate and succeed in the short and medium term.

RECOMMENDATION: The Standing Committee must engage with the DTI and strongly recommend that Once Empowered, Always Empowered principle be explicitly outlawed in the BBBEE Act as amended.

4. Market Concentration and Collusion

A. The South African Financial Services Sector market structure is dominated by big players, all its main sub-sectors are arranged in oligopolistic structures, the so-called BIG 4s.

B. **Bank Collusion** - the Competition Commission referral of the alleged offending banks to the Competition Tribunal must shed light on the Financial Sector compliance with various banking governing policies such as the Third Basel Accord and the Financial Markets Act No 19 of 2012. In addition, bring to the fore the clandestine manner in which banks operate in order for there to be more transparency in the banking system.

C. The new criminalisation section makes it an offence for a director of a firm or a person having or purporting to have management authority in a firm to cause the firm to engage in, or knowingly acquiesce to the firm engaging in, collusive conduct. "Knowingly acquiesce" is defined in the section as "having acquiesced whilst having actual knowledge of the relevant conduct by the firm".

D. Section 73A is thus not only applicable to individuals who actually cause a firm to engage in collusive conduct, but applies equally to those who have actual knowledge of such conduct and turn a blind eye.

RECOMMENDATION: BMF is of the view that should criminalisation of such conduct be applicable in terms of the recent introduction of section 73A of the Competition Act, the Commission and the National Prosecuting Authority should seek that such sanctions are additionally imposed.

5. Skills Development

A. The EEC Report of 2016 indicates that the Financial Services Sector is not making any meaningful progress to break free from the Apartheid-era workforce profile.

B. The Sector has not invested heavily at building critical skills in the right areas of the business, at the right pace and scale so as to create critical-mass.

6. Employment Equity

A. The EEC Report of 2016 indicates that the Financial Services Sector is not making any meaningful progress to break free from the Apartheid-era workforce profile. The EEC Report shows that relative to Economically Active Population (EAP):

- Top Management roles are still dominated by White citizens at **68.4 %**
- Senior Management roles are also dominated by White citizens at **60.6%**
- Professionally Qualified and Specialist roles are equally dominated by White citizens at **46.7%**

B. These statistics are occurring at end of the five year Employment Equity Plans of the Sector. The self-imposed targets have been missed!

7. Enterprise and Supplier Development

C. **The inclusion of Black People** in Panels of Lawyers, Conveyancers and Insurance Claims' Service Providers is only meant to serve as a smoke-screen, black people are never assigned work by the Financial Services Sector. Where they do get work, it is never at a meaningful scale.

D. **Cash Management Services:** There are no serious Black owned and controlled companies providing services such as ATM solutions and Card Supplies to the Financial Services Sector, yet this is a significant part of the value-chain of the sector.

8. Ownership

A. Capital Ownership is the first amongst equals in factors of production and an anchor for enterprise. It is causal in nature, all other factors are beholden to equity owners who, through their voting powers determine the board composition, the Chairman and the CEO and by extension the strategy which the enterprise shall pursue. Including whether it pursues true transformation or not.

B. Due to the strategic nature of the financial services sector, in particular its impact on broader society and the economy. Its ownership structure must either meet or exceed the BBBEE Generic score card.

C. We had already mentioned that the Draft FSC Code has a 10% target for direct ownership which is below the 25% target in the BBBEE Generic Codes.

D. The CENTRE FOR ECONOMIC DEVELOPMENT AND TRANSFORMATION has argued in its submission on the Draft FSC to DTI last year (2016) that the "draft [FSC] allow companies to use indirect ownership to meet the 25% ownership target. Again, this is not allowed under the BEE Codes. Indirect ownership occurs where an institution or other investor owns shares in a company on behalf of beneficiaries and there may not be direct participation by the beneficiaries in the voting rights."

E. For a while, Investec Bank had a 25% direct ownership deal without any of the negative consequences purported to be inherent when black people own a direct stake in a bank which makes them to become the so-called 'shareholder of reference'.

RECOMMENDATION: The Standing Committee must engage with the DTI and strongly recommend that Direct Ownership must be 25% across the board in the Financial Services Sector.

9. Twin Peaks

A. The BMF acknowledges the need to safeguard the interests of depositors and investors in the Financial Services Sector in particular and the economy generally through the Framework covering both Prudential and Market Conduct standards and practices.

B. We are however concerned about the unintended consequences that the Twin Peaks and its associated legislation in the Insurance Industry may have a net effect of imposing barriers of entry in a sector that is already refusing to transform.

C. Amongst the untended consequences, the Twin Peaks and the associated Insurance Bill could:

- sterilise resources by focusing on imaginary instead of real risk.
- increase systemic risk as it seeks to promote only big players.
- cause the Insurance and Retirement Fund prudential management to take a second place to Banking prudential management.

RECOMMENDATION: The Standing Committee must engage with the National Treasury and strongly recommend that a phased approach of the Twin Peaks be adopted for the second tier financial institutions (small players).

10. Market Conduct

There is anecdotal evidence that the Financial Services Sector engages in practices of racial-profiling in its methods and tools it uses to determine, amongst others:

A. **Product and Credit Pricing** - additional premium spreads are added when pricing products for and extending credit to black people, this - if proven, could uncover massive costs to economy due to additional burden and indebtedness of the majority of citizens.

B. **Product Suitability** - marketing the right product to the right target market.

C. **Product Distribution** - purposeful under-servicing of rural and township areas by not allocating services channel infrastructure and/or promoting affordable technologies for the poor to access financial services.

D. **Financial Inclusion** - the sector killed the affordable Mzansi account solution for the poor and there is no serious and sustained marketing campaign in the sector to promote the government backed Masifunde Fund.

11. Conclusion

A. The Financial Services Sector increases the cost of doing business in South Africa due to its low base for ethical market conduct, its disregard for the poor and for corporate governance.

B. We maintain that the industry should strive to meet the BBBEE Generic Code targets. In the absence of progress over many years now, the BMF suggests that the upcoming Financial Services Sector Summit be focused on key principles and that concrete agreements be undertaken to transform the sector once and for all.

C. The Competition Commission should institute a series if sector inquiries on the issues we highlighted under Market Conduct. See point 10 (A, B, C and D) above.

D. The Standing Committee should strongly recommend a Sector Wide Judicial Commission of Inquiry on the alleged practices pertaining to Market Conduct. See point 10 (A, B, C and D) above.