TRUSTEE

TUTOR

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Trustee Tutor 28: Investment platforms and licensing

Retirement funds don't usually manage shares, run trading systems, value investment portfolios, calculate investment performance or operate investment platforms themselves. Instead, they appoint specialist service providers to do this work.

These providers can include discretionary investment managers, hedge fund managers, collective investment schemes, investment administrators, custodians, linked investment service providers (LISPs), insurers, stockbrokers and investment consultants.

For trustees, the key issue is that every provider must be properly authorised to do the work they do. A well-known name, good past investment performance or a long relationship with the fund is not enough.

The fund should be able to identify:

- What service the provider performs
- Which licence or authorisation it has
- Which regulator oversees it
- Whether its licence covers the service it provides
- Who is legally responsible if something goes wrong
- Which assets, records and member data the provider controls
- Which other businesses or subcontractors support the provider

Licensing is an important form of investor protection. It is a public check that takes place before a provider can offer regulated financial services. It requires firms and individuals to meet standards of honesty, skill, operational ability and financial soundness.

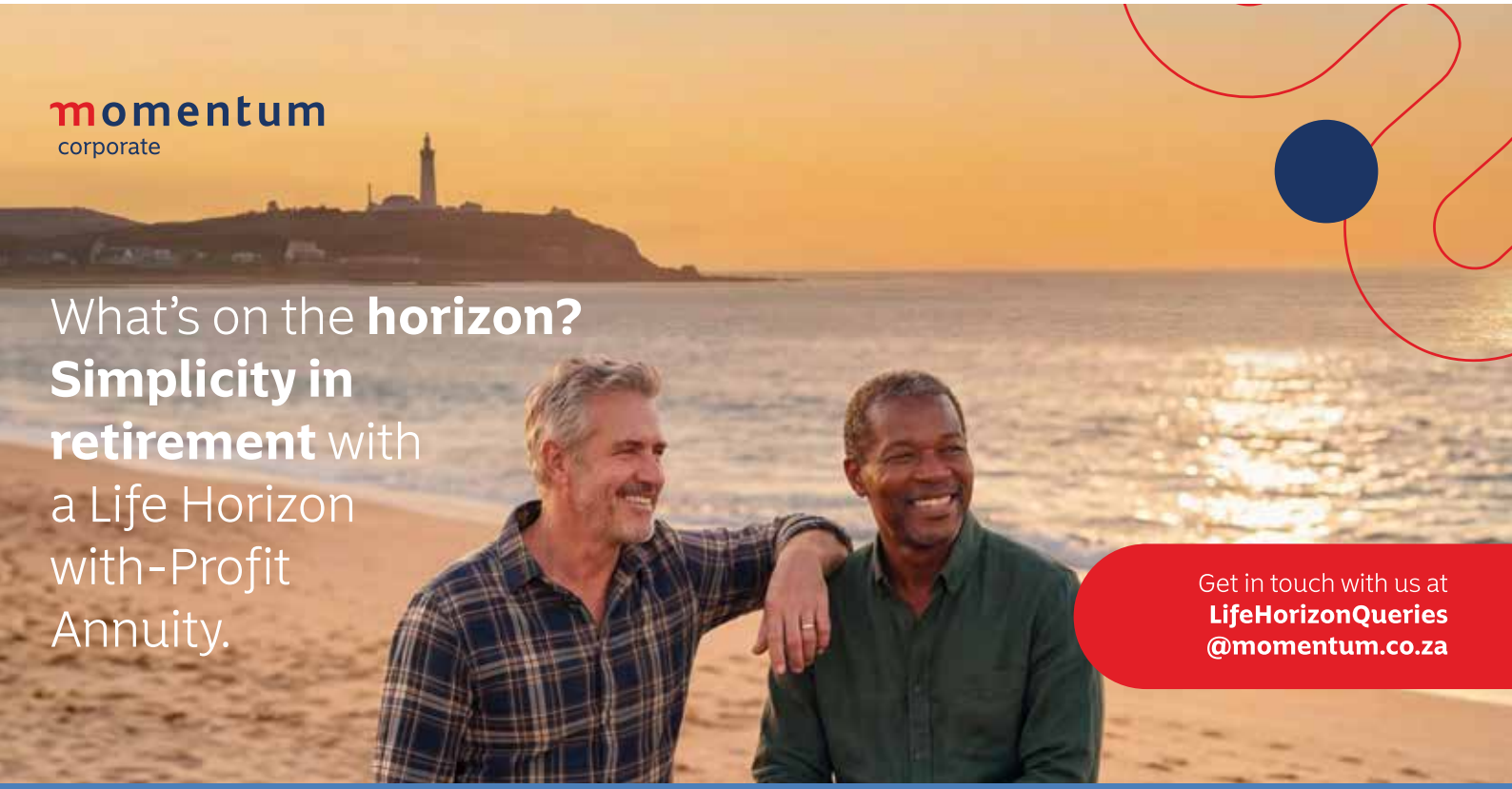
Licensing also means providers are monitored and supervised. A provider or individual can be inspected, fined, restricted, suspended or removed from the market if they don't meet regulatory standards.

This matters because trustees are usually part-time fiduciaries. They must govern the fund responsibly, but they are not expected to run a trading desk, price complicated investments, check international trades or manage cybersecurity systems.

The fund's role is therefore twofold:

1. **Appoint the right regulated provider for each job.**
2. **Monitor whether the provider's legal, contractual and operational protections are working properly.**

A licence does not guarantee good investment returns or stop market losses. But it does create accountability. It reduces the risk that retirement savings are handled by providers that are unqualified, poorly supervised or financially weak.



The regulatory framework

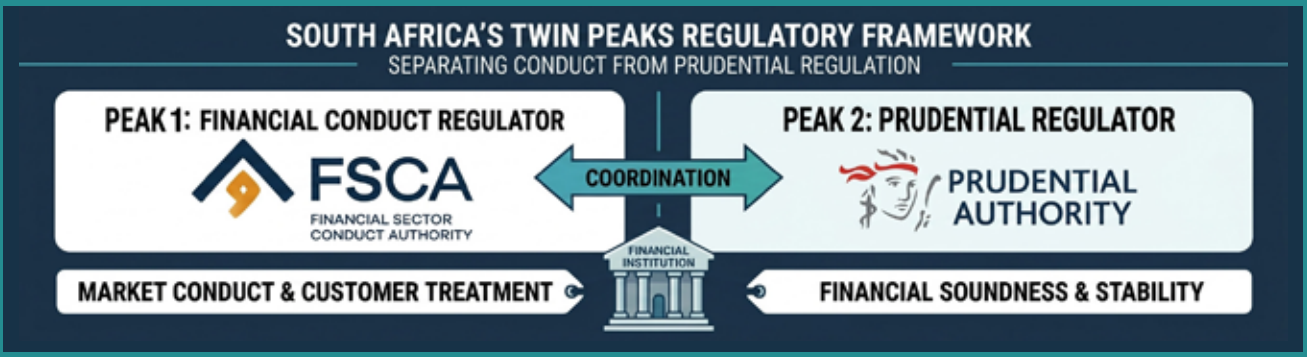
South Africa's financial sector regulation follows the Twin Peaks model. This separates regulation of financial conduct from regulation of financial strength and stability.

The Financial Sector Conduct Authority, or FSCA, is the main conduct regulator. It licenses Financial Services Providers under the Financial Advisory and Intermediary Services Act, known as FAIS. It also authorises collective investment scheme managers under the Collective Investment Schemes Control Act, or CISCA.

The FSCA oversees conduct, disclosure, conflicts of interest, customer treatment, market behaviour and certain operational standards.

The Prudential Authority, which sits within the South African Reserve Bank, oversees the financial strength of insurers, banks and some other financial institutions.

This is especially important when a retirement fund invests through an insurance policy, a smoothed-bonus product or another product issued by an insurer. In these cases, the fund's legal claim is against the insurer. The insurer's capital, solvency and governance requirements therefore become an important protection.



This table gives you the full picture of the supervisory bodies that monitor a fund's investment managers, and the role they play, creating several layers of protection around retirement assets.

Authority	Relevance for investment suppliers and funds
FSCA	Licences and supervises FSPs, including Category I, II, IIA and III providers; authorises CIS managers; enforces financial conduct standards
Prudential Authority	Licences insurers and regulates their capital, governance, outsourcing and financial resilience
Financial Intelligence Centre	Enforces anti-money-laundering duties under FICA, including due diligence, sanctions screening and suspicious transaction reporting
Information Regulator	Enforces POPIA, including controls over member and beneficiary data handled by managers, platforms, consultants and investment administrators
FAIS Ombud	Resolves qualifying complaints about financial advice and intermediary services
Pension Funds Adjudicator	Resolves complaints relating to retirement funds and can issue determinations with the force of civil judgments
National Treasury and SARS	Shape tax, exchange control and offshore investment structures

Investment manager licences

Here are some practical examples you might have experienced of regulation and licensing in action:

A discretionary manager is regulated for how it manages an investment mandate.

A CIS manager is regulated for how it runs a unit trust.

A custodian may provide independent safekeeping of assets.

A platform may be licensed to provide financial-services administration.

An insurer must meet prudential requirements.

Trustees should not assume that one licence covers every service in the investment chain.

Category II: Discretionary financial services

A discretionary investment manager that makes investment decisions for a retirement fund will generally need a Category II Financial Services Provider licence.

Discretionary management means that the fund gives the manager authority to make investment decisions within an agreed mandate.

For example, a fund may approve a balanced portfolio mandate. The mandate may set limits for shares, bonds, offshore assets, property and alternative investments. The manager can then choose individual shares, unit trusts or other investments, as long as it stays within those limits.

The investment manager does not have unlimited freedom. It must follow:

The investment mandate

Regulation 28 limits and other relevant laws

The conditions attached to its licence

The FAIS General Code of Conduct



For local discretionary managers, the FSCA generally expects a real South African operating presence. It also expects investment decisions to be made from South African offices. This helps make regulatory oversight meaningful.

A manager should not have only a marketing office in South Africa while important investment decisions are really being made elsewhere, without the right arrangements and disclosure.

The FAIS General Code requires managers to act honestly, fairly and with proper skill, care and diligence. They must manage conflicts of interest, keep proper records, separate client assets from their own assets, deal correctly with client money and have professional indemnity and fidelity insurance where required.

These duties apply even if the investment management agreement does not mention them. A strong contract is still important, but a manager cannot escape its regulatory duties because a contract is silent on a particular issue.

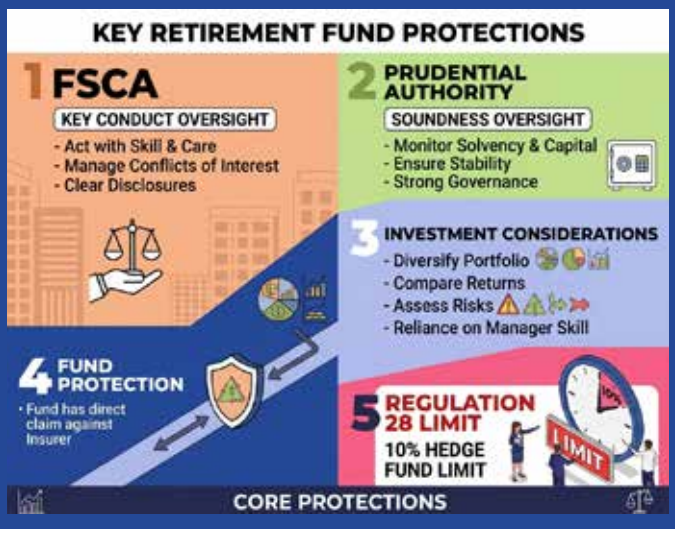
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Category IIA: Hedge Fund Management

Hedge fund managers generally need a Category IIA licence.

Hedge funds may use more complicated investment strategies, including derivatives, borrowing or leverage, short selling, relative-value trades and other non-traditional investments.

A hedge fund investment can help diversify a portfolio or provide returns that are different from traditional shares and bonds. But it also brings more complex risks that trustees and investors should be aware of, for example, liquidity, valuation and operational risks, to name a few. Investors in hedge funds also have greater reliance on the manager's skill and controls. Because of this, Regulation 28 limits a retirement fund's investment in hedge funds to 10%.



Category I: Investment advice and consulting

A provider that gives investment advice or intermediary services will need Category I authorisation under FAIS.

Investment consultants, employee benefit advisers and financial planners may fall into this category when they recommend asset allocation, investment managers, default portfolios, life products, retail retirement products or investment platforms.

The difference between Category I and Category II is important:

- A Category I provider may recommend an investment solution.
- A Category II provider may make investment decisions for the fund within an agreed mandate.

A consultant should not quietly move from giving advice to making investment decisions without the correct licence and mandate.



Trustees should be clear about whether a provider is recommending, implementing, monitoring or actually making decisions.

FAIS requires advisers to manage conflicts of interest, give suitable information and keep records showing the basis for their advice. This helps trustees make better decisions and creates a record of why an investment manager, platform, product or strategy was recommended.

Trustees should ask:

- Is the consultant authorised for the relevant product category?
- Does it receive fees from investment managers, insurers or platforms?
- Does it recommend products from related companies?
- Is its manager-selection process documented?
- Does it assess fees, risk, performance, service quality and governance?
- Can it explain why a recommended manager suits the retirement fund?
- Does it clearly separate advice from discretionary management?



Investment platforms and legal structures

An investment platform is not simply a technology system. It forms part of a regulated financial services structure.

A platform may give access to several investment products, combine reporting, process transactions, allocate cash, keep records and support member investment choice.

The structure a fund uses affects:

- How easily assets can be sold
- How well investors are protected
- Who legally owns the assets
- How clear the information and fees are
- Which risks the fund still carries

Vehicle or structure	Regulatory architecture	Main advantages	Main limitations
Segregated mandate	Category II manager, usually with independent custody or nominee arrangements	Bespoke mandate, strong transparency, fund level control	Requires scale and governance capability
Unit trust / CIS	CISCA-authorised manager and independent trustee or custodian	Diversification, liquidity, ring fenced scheme assets	Less customisation and need for Regulation 28 look-through
ETF / index fund	CIS manager or issuer plus exchange and authorised user infrastructure	Low cost, transparent holdings, efficient market access	Tracking difference, trading costs and index concentration
Life policy or smoothed-bonus product	Prudential Authority-licensed insurer	Pooling, smoothing, possible guarantees	Insurer credit and product complexity risks
LISP / wrap platform – more for retail investors	Typically Category III administrative FSP, possibly with Category I advice functions	Consolidated reporting and investment menu	Fee stacking, restricted choice and operational dependency
Private equity, hedge funds, infrastructure	Category II or IIA manager, with complex underlying structures	Potential diversification and long-term return opportunity	Illiquidity, difficult valuation and higher governance burden

Segregated mandates

A segregated mandate is a portfolio managed specifically for a retirement fund. The fund appoints a Category II manager and agrees an investment mandate designed for that fund only.

The fund has complete flexibility to set the investment limits, benchmark, risk controls, reporting requirements, responsible-investment principles, proxy-voting expectations, liquidity rules and fee structure. This makes segregated mandates attractive for larger funds with strong governance resources.

The underlying assets are normally held for the fund through a custodian or nominee. This creates an important separation between the investment manager and the assets.

The main benefits are customisation, transparency and control. The fund can see what it owns and negotiate the mandate directly.

The main drawbacks are the need for scale, higher governance demands, the risk involved in changing managers and the need to monitor the mandate closely.

Collective investment schemes

A collective investment scheme, commonly known as a unit trust, pools money from many investors into a portfolio managed by a CIS manager.

A key protection is that the scheme's assets are ring-fenced from the manager's own balance sheet. An independent trustee or custodian has an oversight role. This separation is valuable if the manager experiences financial problems.

Unit trusts are often useful building blocks for diversified portfolios. They can be accessible to smaller funds and umbrella fund arrangements. They usually offer regular pricing, liquidity and standardised reporting. Trustees must still look through the unit trust's underlying investments for Regulation 28 purposes.

The trade-off is that the fund owns units in the scheme rather than a portfolio designed specifically for it.



ETFs and index funds

ETFs and index funds provide relatively low-cost access to specific markets or indices. Their benefits can include transparent holdings, broad diversification and lower stated management fees than many actively managed strategies.

They may work well as a core part of a portfolio. But trustees should not choose an ETF only because it has a low total expense ratio.

An ETF that tracks a highly concentrated index may be cheap, but it can still create significant concentration risk. Low cost is useful only if the investment exposure suits the fund's strategy.

Life policies and smoothed-bonus products

Life insurers can issue investment policies, pooled products and smoothed-bonus portfolios. In these structures, the retirement fund usually has a contractual claim against the insurer. It does not directly own the underlying assets.

Potential benefits include pooling, smoother returns and certain guarantees. These features may be useful for older members, defined benefit liabilities or funds trying to smooth out investment performance volatility.

But the fund must understand what it gives up. It may have less transparency, less flexibility and less ability to see underlying charges. Trustees should also consider any product terms that include market-value adjustments, insurer discretion over bonus allocations, limits on exiting the product or conditions attached to guarantees.

The insurer's capital and solvency rules offer protection. But the product is not risk-free. The fund may reduce visible market volatility while taking on insurer credit risk, product complexity and lower expected long-term returns.

Linked investment platforms

A LISP, or wrap platform, is often used to give access to several unit trusts, life funds or other investment products through one administrative system. It can combine statements, process investment switches, provide online tools and simplify recordkeeping.

The platform may be licensed as a Category III administrative FSP. If related parties provide investment advice, Category I licensing may also be needed.

Platforms can be useful where a fund or financial planner needs efficient administration across several underlying products. However, trustees should look carefully at the total fees, which may include:

- A platform fee
- Underlying fund-management fees
- Transaction costs
- Advice fees
- Possible insurance-wrapper charges
- Switching costs or exit charges in some cases

A platform may also limit the range of available funds or direct users towards products from related businesses.



Investor protection and trustee responsibilities

The regulatory system protects members and investors through several layers.

1. **Fit-and-proper requirements aim to keep unsuitable firms and individuals out of the market.**

2. **Conduct rules require investment managers and advisers to act fairly, disclose conflicts and keep proper records.**

3. **Client assets should be protected through segregation, custody, nominee arrangements and the ring-fencing of CIS assets.**

4. **Insurers are subject to prudential rules, including capital and governance requirements.**

5. **FICA helps reduce the risk that investment products and financial systems are used for money laundering, sanctions evasion or other illegal activity.**

6. **POPIA and cybersecurity standards protect member and beneficiary information. Investment managers, platforms, consultants and administrators often handle sensitive personal and financial data. They need suitable safeguards, incident-response plans, access controls and data-processing arrangements.**

Regulators can impose serious penalties for misconduct. These can include administrative fines, licence suspension, licence withdrawal, debarment and, in some cases, criminal penalties.

However, regulatory enforcement does not mean trustees can sit back and do nothing. The board remains responsible for appointing suitable providers, responding to warning signs and monitoring service quality.

Conclusion

Investment managers and investment administrators are central to the retirement fund system. Their licences, regulatory duties, operational controls and contracts are meant to protect members' money and information.

A Category II licence is key for discretionary investment management. Category IIA applies to hedge-fund management. Category I is generally relevant for investment advice and consulting. Category III is important for administrative platform activities, including certain LISP and investment administration functions.

CIS managers, insurers, custodians and stockbrokers also operate under their own additional legal frameworks.

Trustees do not need to become investment professionals, technology specialists or lawyers. But they do need to understand the regulated chain behind every investment decision and every investment record.

That means knowing:

- Who makes investment decisions
- Who holds the assets
- Who values the assets
- Who reconciles the records
- Who calculates the fees
- Who provides the platform
- Which licence applies to each activity
- What rights the fund has if the relationship fails

The best protection is not a licence on its own. It is the combination of the right licence, a clear mandate, independent custody, reliable investment administration, transparent fees, strong cyber controls, proper contracts and active trustee oversight.

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Assessment questions

How to?

The assessment for this issue of Trustee Tutor follows for information and/or training purposes. If you would like to earn verified CPD hours for reading this issue, please go to www.pensionsworldsa.co.za/cpd-portal/ and complete the assessment electronically to recieve your certificate immediately on meeting the competency requirements.

1. What is the main purpose of licensing investment service providers?

a. To guarantee that providers will outperform their investment benchmarks ☐
b. To confirm that providers meet regulatory standards before offering services ☐
c. To allow trustees to delegate all responsibility for fund investments ☐
d. To ensure every provider uses the same investment strategy ☐

2. Which regulator is mainly responsible for conduct regulation and FAIS licensing?

a. The Financial Sector Conduct Authority ☐
b. The Prudential Authority at the Reserve Bank ☐
c. The Pension Funds Adjudicator ☐
d. The Financial Intelligence Centre ☐

3. What type of FAIS licence would a discretionary investment manager generally need?

a. Category I, for investment advice and intermediary services ☐
b. Category II, for discretionary financial services ☐
c. Category IIA, for hedge-fund management services ☐
d. Category III, for administrative platform services ☐

4. What distinguishes a Category II manager from a Category I investment consultant?

a. A Category II manager may only recommend investment managers ☐
b. A Category I consultant may trade assets without instructions ☐
c. A Category I consultant must provide custody of fund assets ☐
d. A Category II manager may make decisions within an agreed mandate ☐

5. Why must trustees look through a unit trust's underlying investments?

a. To calculate the investment manager's annual performance fee ☐
b. To assess the fund's compliance with Regulation 28 limits ☐
c. To determine whether the unit trust is listed on an exchange ☐
d. To confirm the identity of each unit trust investor ☐

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6. Which licence category generally applies to hedge-fund management?

a. Category I, because hedge funds mainly provide investment advice ☐
b. Category II, because hedge funds only hold client assets ☐
c. Category IIA, because hedge funds use more complex strategies ☐
d. Category III, because hedge funds mainly perform administration ☐

7. What is a key protection offered by a collective investment scheme?

a. The manager guarantees investors a minimum annual return ☐
b. Investors can dictate every individual investment purchase or sale ☐
c. The scheme is exempt from Regulation 28 investment limits ☐
d. Scheme assets are ring-fenced from the manager's own balance sheet ☐

8. In a life policy investment structure, what does the retirement fund usually hold?

a. Direct legal ownership of every underlying investment asset ☐
b. A contractual claim against the insurer that issued the policy ☐
c. A membership interest in the investment manager's business ☐
d. A shareholding in the custodian that holds the assets ☐
e.

9. Which risk should trustees consider when using a linked investment platform?

a. The platform may create fee stacking across several service layers ☐
b. The platform automatically removes all investment concentration risk ☐
c. The platform guarantees unrestricted access to every available fund ☐
d. The platform replaces the need for investment governance oversight ☐

10. Which combination best describes effective protection for retirement fund assets?

a. A well-known provider, strong past returns and low investment fees ☐
b. A licence alone, supported by annual trustee meeting attendance ☐
c. The right licence, clear mandate, custody and active oversight ☐
d. A single platform, a broad investment menu and market guarantees ☐