

# NATIONAL RESERVE BANK OF TONGA

## Prudential Statement No.8 **Revised 2014**

### FIT & PROPER REQUIREMENTS

#### Introduction

1. This Statement is issued in terms of Section 15(3) of the Financial Institutions Act 2004 (the “Act”).
2. This Statement aims to ensure that a licensed financial institution (LFI) is well managed and that persons occupying key positions within the institution have the degree of probity and competence commensurate with their responsibilities. These key positions include directors and senior managers as defined in this Statement. Many of the factors outlined in this Statement are also applicable to the assessments of whether a person, company or partnership are fit and proper to acquire or retain a substantial shareholding in a licensed financial institution.
3. A number of provisions of Act, which are outlined below, give rise to fit and proper considerations. Specifically:
  - Section 7 of the Act indicates that in considering an application for a licence under Section 6 the Reserve Bank shall have regard to:  
*“the ability of the applicant to carry on the proposed business, the character and experience of its directors and management, and those persons who will own 10 percent or more of the voting shares of the applicant”*.
  - Section 14 of the Act requires Reserve Bank approval to be obtained prior to any transfer of control of a licensed financial institution. The Reserve Bank when assessing any such application will give consideration to those criteria outlined in Section 7 of the Act.
  - Section 23 of the Act requires a licensed financial institution with the consent of the Reserve Bank to appoint an external auditor for each financial year.
  - Section 26 of the Act provides that certain persons are disbarred from serving as directors or management of a licensed financial institution.
4. It is also clear that the actions of, and decisions made by, directors and management have significant implications for the on-going sound and prudent management of a LFI and that the fit and proper requirements must be met on an on-going basis.

#### Policy

5. The Reserve Bank expects that licensed financial institutions will have in place policies and procedures that ensure that, auditors, directors and management have the degree of probity and competence commensurate with their responsibilities and may require a LFI to demonstrate that it has made appropriate enquiries in respect of key appointments.
6. At a minimum each LFI should have in place policies and procedures to address the fit and proper principles and criteria contained in this Statement and determine whether a person is a disbarred person in terms of the Act.

7. More generally, in addition to having in place policies and procedures to address the fit and proper principles for directors and management, LFIs should put in place screening procedures to ensure high standards when hiring employees at all levels and to prevent the employment of persons convicted of offences involving fraud and dishonesty. Employee screening procedures should ensure that:
  - a. Employees have a high level of competence necessary for performing their duties;
  - b. Employees have appropriate ability and integrity to conduct the business activities of the financial institution;
  - c. Potential conflicts of interests are taken into account, including the financial background of the employee;
  - d. Persons charged or convicted of offences involving fraud, dishonesty or other similar offences are not employed by the LFI.
8. The policies and procedures referred to in paragraph 6 must include review of the fitness and propriety of directors and management on at least an annual basis. Written documentation detailing the LFIs review and assessment of the fitness and propriety of persons covered under this Statement should be maintained and made available to the Reserve Bank on request.

### **Management**

9. For the purposes of this Prudential Statement “management” includes:
  - a. the Chief Executive;
  - b. the Country Head of a foreign incorporated LFI;
  - c. the senior officer outside Tonga with responsibility for overseeing the Tongan operations of a foreign incorporated LFI;
  - d. managers reporting directly to the Chief Executive or Country Head;
  - e. managers with direct or matrix reporting responsibilities offshore.

### **Fit and Proper Criteria**

10. Determining whether a person is “fit and proper” involves assessing whether the person has appropriate technical competence, by reference to attributes such as education, knowledge, skills and experience, and is of good fame and character, by reference to attributes such as diligence, honesty, integrity, judgement and reputation.
11. It is necessary to consider the fitness of a person with reference to the position that the person holds or is being considered for. A decision that a person is not fit for a particular role does not automatically exclude them from other roles. However, where a person is found to be not “proper” due to a lack of diligence, honesty, or integrity, or because of poor judgment or poor reputation, it will normally be the case that the person will not be suitable for any position.
12. In addition to the requirements of Section 26 of the Act, the criteria for fitness and propriety include, but are not limited to:

- a. Whether the person has the educational or technical qualifications, knowledge, skills, experience, competence, diligence, judgment, character, honesty, or integrity required to satisfactorily discharge the responsibilities of the position<sup>1</sup>;
- b. Whether the person has failed to discharge his or her responsibilities as a director or manager of, or a professional service provider to any entity with competence, diligence, sound judgment, honesty, or integrity<sup>2</sup>;
- c. Whether the person has been the subject of criticism, discipline, punishment, or adverse findings, directions or orders, by a court, tribunal, official inquiry, regulatory agency, complaints handling body, dispute resolution body, or professional or industry body;
- d. Whether the person has been subject to any adverse finding or settlement in civil or criminal proceedings (other than minor traffic offences), or enforcement actions;
- e. Whether the person or an entity with which they were associated was expelled or excluded from, or refused admission to, a professional or industry body, or a clearing house or exchange;
- f. Whether the person or an entity with which they were associated was refused a licence or authorisation relating to a commercial or professional activity, or had such a licence or authorisation revoked;
- g. Whether the person was terminated, resigned or was asked to resign, from a position as director or manager of, or professional service provider to, an entity in circumstances which reflected adversely on his or her competence, diligence, judgement, honesty, or integrity in discharging his or her responsibilities in the position;
- h. Whether the person was disqualified, removed or excluded from, or not admitted to the management of an entity or class of entities or a commercial or professional activity by a court, tribunal or regulatory agency, or by the operation of a legislative provision
- i. Whether the person seriously or persistently failed to manage his or her debts or financial affairs satisfactorily in circumstances where such failure caused loss to others;
- j. Whether the person was, or acted as, a director or manager of, or a professional service provider to, an entity which was, or later came to be, insolvent, under insolvency administration, statutory or judicial management or failed to meet its financial obligations to, creditors or beneficiaries;
- k. Whether the person contravened any regulatory requirement or professional standard relating to the management of an entity; or commercial or professional activities;
- l. Whether the person was obstructive, misleading or untruthful in dealing with a court, tribunal, official inquiry, complaints handling body, dispute resolution body, professional body, industry body or regulatory agency
- m. Whether the person demonstrated a lack of readiness and willingness to comply with legal obligations, regulatory requirements or professional standards;

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<sup>1</sup> This could include reference checks, reviews of academic transcripts and work history.

<sup>2</sup> Other considerations could include the person's work ethic.

- n. Whether the person breached a fiduciary obligation or other obligation involving trust;
  - o. Whether the person perpetrated or participated in negligent, deceitful, or otherwise discreditable business or professional practices;
  - p. Whether the person failed to disclose a conflict of interest, failed to disqualify himself or herself because of a conflict of interest, participated in deliberations relating to a matter in which he or she had a conflict of interest; or acted in his or her own interests in preference to the interests of others contrary to a legal, professional or ethical obligation which applied to the person;
  - q. Whether the person has a conflict of interest which may influence his or her ability to carry out the role and functions of the position they are being considered for, or already fill;
  - r. Whether the person knowingly appointed a person who was not fit and proper to act as an alternate director or manager;
  - s. Whether the person is of bad repute in any business or financial community or any market.
13. These criteria may not be exhaustive or definitive. Anything – in Tonga or elsewhere - which suggests that approval of a person may harm customers or the stability of the LFI is relevant, whether or not it can be subsumed under the foregoing elements.

**Additional criteria applying to significant shareholders**

- 14. Many of the factors listed in paragraph 12 apply equally to the assessments of whether a person, including a corporation, company, partnership or other legal entity, are fit and proper to acquire or retain a significant shareholding<sup>3</sup> in a LFI.
- 15. In addition the Reserve Bank will need to be satisfied that the significant shareholder, or proposed shareholder, has financial resources sufficient to support the licensed financial institution as necessary in meeting continuing capital requirements. In this regard, the Reserve Bank expects:
  - a. To be informed of any significant development adversely affecting the parent institution's or substantial shareholder's financial soundness and/or reputation; and
  - b. To be provided promptly with copies of audited financial accounts and significant media releases (for example, announcements of changes in strategy or decisions to offer new services which may impact on the LFIs operations in Tonga).

**Additional criteria applying to directors**

- 16. No director serving on the board of a locally-incorporated LFI operating in Tonga should simultaneously serve as a director on another LFI operating in Tonga or be directly or indirectly affiliated in any way with another LFI operating in Tonga, including through ownership, management or employment.

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<sup>3</sup> A "significant shareholding" for purposes of this Statement includes any person, including any corporation, company, partnership or other legal entity, that directly or indirectly owns or has a beneficial interest in 10% (ten percent) or more of the voting shares of the LFI..

## Eligibility Criteria for External Auditors

17. In addition to the general criteria in paragraphs 10, 11 and 12 above, which must be met by the auditing firm and the partner responsible for the audit, the partner and members of the audit team:
  - a. Must not be a director or employee of the LFI or of a related body;
  - b. Must have appropriate formal qualifications and be a member of a recognised professional body;
  - c. Must have a minimum five (5) years experience in auditing in the banking and finance industry.

## Information to be provided to the Reserve Bank

18. LFIs are required to provide the Reserve Bank with all relevant details in respect of their shareholders, directors, managers and auditors<sup>4</sup> as set out in paragraphs 19 to 21 below.
19. A LFI must ten (10) business days prior to nominating or appointing a person covered by this Statement, notify the Reserve Bank in writing of the proposed appointment and include information such as details of the individual's name, qualifications, membership of professional associations, history, current business or other professional associations and full curriculum vitae, together with an affirmation that the person complies with the financial institution's fit and proper criteria. The Reserve Bank may make additional enquiries, or require the LFI to make other reasonable enquiries and provide information and documentation to the Reserve Bank. The Reserve Bank reserves the right to require the proposed appointment to be overturned if the Reserve Bank is of the opinion that the person is not a fit or proper person to occupy the position for which they are being considered.
20. A LFI must notify the Reserve Bank in writing as soon as practicable, and in any event not later than fourteen (14) days after the occurrence of any of the following **except new appointment**:
  - a. Changes in persons covered by this Statement, including any resignation, retirement or removal of a person. Notification of a change must include the following:
    - (i) for resignation, retirement, or removal of a person covered by this Prudential Statement the reasons for the resignation, retirement or removal.
  - b. Changes in the LFI's on-going assessment of the fitness and propriety of a person covered by this Prudential Statement. Where the LFI determines that the person does not meet one or more of the fit and proper criteria in respect of the position they occupy it must provide particulars of the issue to the Reserve Bank as well as the action it is taking to address the matter.
21. The Reserve Bank may require a LFI to provide a copy of its Fit and Proper policy and procedures along with **copies of the LFIs written** assessment in particular cases, including the information/documentation relied upon to form a judgement as to the fitness and proprietary of an individual.
22. The LFI must provide the Reserve Bank with an annual declaration that it has appropriate Fit and Proper policies and procedures in place and that all persons covered

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<sup>4</sup> Section 23 of the Act provides that a licensed financial institution shall, with the consent of the Reserve Bank, appoint an external auditor for each financial year.

by this Prudential Statement remain Fit and Proper and are not disbarred in terms of section 26 of the Act. This should be supported by a complete list of the relevant persons and their position/roles. This information must be provided to the Reserve Bank not more than 14 (fourteen) calendar days after the LFI's year-end.

### **Removal of Persons**

23. Notwithstanding the emphasis on institutional self assessment in respect of fit and proper requirements, the Reserve Bank may, in terms of section 33 of the Act, direct a LFI to remove an auditor, director or manager where it finds that such a person is disbarred in terms of the legislation or it has concerns about fitness and propriety.
24. Alternatively, the Reserve Bank may impose conditions that relate to the areas or activities in which the individual can work, further training the individual needs to undertake, or specific reporting or other requirements that the Reserve Bank believes are necessary and appropriate in respect of the appointment. Any failure to meet these conditions could result in a direction for the removal of the individual.
25. A person or institution affected by a decision made by the Reserve Bank referred to in paragraphs 23 and 24 may request that the Reserve Bank to review that decision. The onus is on the person or institution to demonstrate that he or she is fit and proper to carry on the business concerned, or exercise the responsibility proposed; the Reserve Bank does not have to prove that a person is not fit and proper.
26. Applications for review of the fitness and propriety of an individual should be directed to the Governor, National Reserve Bank of Tonga.

### **Compliance with Prudential Statement No. 8**

27. This statement is effective from **1 May 2014**. Non-compliance with the requirements of this Prudential Statement will be subject to corrective actions as provided under section 33 of the Financial Institutions Act 2004 and the administrative penalties outlined in Prudential Statement No.3 Administrative Penalties.

National Reserve Bank of Tonga

**April 2014**