



Office: 010 597 0835 | Facilitator: 083 821 8801 | E-mail: [anna@compliancelearningcenter.net](mailto:anna@compliancelearningcenter.net)

Website: [www.compliancelearningcenter.net](http://www.compliancelearningcenter.net) |

Address: 10A Lever Street Brackenhurst Alberton, South Africa

Registration nr: 2018/242685/07 | Vat nr: 4070281904

# Study Guide

**THE FINANCIAL MARKET ACT: ONLINE CPD COURSE 2020 / 2021**

*January 2021*

*© Compliance and Learning Center (Pty) Ltd*



## Course summary

The Financial Markets Act (Act no. 19 of 2012) provides for regulation of the financial markets in South Africa. The course provides a brief introduction to the Act and thereafter consider the requirements and responsibilities imposed on the role-players regulated in terms of the Act. The course concludes by considering the stipulations to prevent market abuse and insider trading.

## Time allotted for course

The course consists of 3 topics with an assessment that needs to be completed. The time allotted for each aspect is as follows:

Topic number	Title	Word count	Level	Time allotted
Topic 1	Introduction to the Financial Markets Act	949	Entry	20 minutes
Topic 2	Requirements and responsibilities of the various role-players	6 823	Entry	165 minutes
Topic 3	Unlawful behaviour in the financial markets	3 604	Entry	85 minutes
	Assessment			

<b>Total time</b>	<b>4.5 hours</b>
-------------------	------------------

## Assessment and certification

After completion of the workshop the learner must complete an electronic assessment on the learning management system.

- **Form of assessment:** Multiple Choice Questions
- **Number of questions:** 20 questions
- **Duration:** 60 minutes
- **Competency mark:** 60%

Upon obtaining a competency mark of 60% the learning will receive a certificate of completion. The learner will be afforded an opportunity to re-do the workshop should a competency mark not be attained.

## **Course accreditation**

**CPD Category:** Online program

**COB Category:** All Classes of Business

**Accreditation valid until:** 11 January 2022

**CPD Points allocated:** 4.50 hours | points on completion and pass of assessment

**IISA Approval number:** EVT-20210105-0001

## Table of contents

<b>Topic 1 Introduction to the Financial Markets Act</b>	<b>4</b>
<b>Topic 2 Requirements and responsibilities of the varioius roleplayers</b>	<b>8</b>
<b>Topic 3 Unlawful behaviour in the financial markets</b>	<b>29</b>

## Copyright notice

© 2021 Compliance and Learning Center (Pty) Ltd

All rights reserved. No part of this publication may be reproduced, distributed, or transmitted in any form or by any means, including photocopying, recording, or other electronic or mechanical methods, without the prior written permission of the author, except in the case of brief quotations embodied in critical reviews and certain other noncommercial uses permitted by copyright law.

For permission request write to the author at the address below:

Compliance and Learning Center (Pty) Ltd  
10A Lever Road  
Brackenhurst  
Alberton  
1449  
South Africa

## Ordering information

If you would like to order the publication, please contact author at address above.

## TOPIC 1 INTRODUCTION TO THE FINANCIAL MARKETS ACT

---

### LEARNING OUTCOMES

After studying the topic, the learner should be able to-

- Name the objectives of the Financial Markets Act.
- Describe the various role-players regulated in terms of the Financial Markets Act.

### 1.1 Objects of the Act

The Financial Markets Act (FMA) objects are significant as it displays the authorities' commitment to adhering to international regulatory standards. The objectives are to-

- Increase confidence in the South African financial markets by:
  - Requiring that services be provided in a fair, efficient and transparent manner.
  - Contributing to the maintenance of a stable securities market environment.
- Promote the protection of regulated persons and clients.
- Reduce systemic risk.
- Promote the international competitiveness of securities services.

### 1.2 Role players and other important definitions

There are various role players that the Act seeks to regulate either directly through the FSCA, or indirectly through a self-regulatory organisations (SRO).

An exchange and a central securities depository (CSD) have the status of an SRO in terms of the Act.

### 1.2.1 Who are the role-players in terms of the FMA?

A list of the role-players and definition of each is tabled in Table 2.1

*Table 1.1: Role-players in terms of the FMA*

<b>EXCHANGE</b>	A person (individual, company or association) that provides the infrastructure for bringing together buyers and sellers of securities and matching orders.
<b>CLEARING HOUSE</b>	A licensed clearing house providing clearing services or settlement services or both.
<b>AUTHORISED USER</b>	A person authorised in terms of the exchange rules to perform securities services.
<b>CENTRAL SECURITIES DEPOSITORY</b>	A licensed CSD providing custody and administration services.
<b>PARTICIPANT</b>	A person that holds in custody and administers securities and has been accepted as a participant by the CSD.
<b>ISSUER</b>	An issuer of securities such as a company issuing shares.
<b>TRADE REPOSITORY</b>	A person who maintains a centralized electronic database of records of transaction of data.
<b>REGULATED PERSON</b>	An exchange, authorised user, CSD, participant or clearing house.

### 1.2.2 What are “securities in terms of the FMA?

The following are deemed securities in terms of the FMA:

- Shares, stocks and depository receipts in public companies and other equivalent equities.
- Notes.
- Derivative instruments (defined as any financial instrument or contract that creates rights and obligations and that derives its value from the price or value, or the fluctuating value that may vary depending on a change in the price or value, of some other particular product or thing, like an index).
- Bonds.
- Debentures.

- Participatory interests in a collective investment scheme as defined in the Collective Investment Schemes Control Act and units or any other form of participation in a foreign collective investment scheme approved by the Commissioner.
- Units or any other form of participation in a collective investment scheme licensed or registered in a foreign country.
- Instruments based on an index.
- The securities that are listed on an external exchange.
- An instrument similar to one or more of the securities listed above declared by the Commissioner by notice in the Gazette to be a security for purposes of this Act.
- Rights in the securities referred to in the above list.

EXCLUDING the following:

- Money market instruments (except for purposes of the custody and administration of securities)
- Any security contemplated in the above list of securities specified by the Commissioner by notice in the Government Gazette.

### **1.2.3 What is “clearing or “clear” in terms of the FMA?**

Before settlement, to determine and calculate the exact number and nominal value of the securities of each kind to be transferred and the amount of money to be paid to ensure settlement.

This includes in some cases the process by which the performance of a transaction is underwritten from the time of trade to the time of settlement.

### **1.2.4 What are “securities services” in terms of the FMA?**

The following are deemed securities services in terms of the FMA:

- Buying and selling of securities.
- Custody and administration of securities.
- Management of securities by an authorised user.
- Clearing of transactions in listed securities.
- Settlement of transactions in listed securities.

### 1.3 Restrictions and Prohibitions on listed securities

The business of buying and selling listed securities may ONLY be conducted by the following persons:

- An authorised user.
- A person effecting the transactions through an authorised user. (This will be a person who is trading as a principal i.e., for own account. Agency trading i.e., trading for clients, may only be conducted by authorised users authorised in terms of the rules of the exchange or financial services providers authorised thereto by the FSCA under the FAIS Act. These financial services providers must also trade through an authorised user.)
- A financial institution transacting with another financial institution on a principal basis This means that financial institutions may trade with each other off exchange with their own funds and assets but not clients' funds and assets. Financial institutions for these purposes include a pension fund, pension fund administrator, friendly society, long-term and short-term insurer and a bank.
- A person who buys or sells listed securities to give effect to: -
  - A reconstruction of a company or group of companies by the issue or reallocation of shares.
  - A takeover of one company by another.
  - An amalgamation of two or more companies.
  - A change in the control over management or the business of a company.

Financial institutions trading off exchange (regardless whether they are conducting the business of buying and selling securities) must report these transactions to the Commissioner.

The Commissioner may prescribe the information required from each transaction and prescribe the manner and time within which the report must take place.

The Commissioner must then disclose this information to the exchange and the public. The exchange may also publish this information.

## TOPIC 2 REQUIREMENTS AND RESPONSIBILITIES OF THE VARIOUS ROLEPLAYERS

---

### LEARNING OUTCOMES

After studying the topic, the learner should be able to-

- Describe the requirement for an exchange to be licensed.
- Outline the requirement and responsibilities imposed on the role-players under the Financial Markets Act.
- Understand Custody and Administration of Securities.

### 2.1 Introduction

The sections following consider the requirement and responsibilities imposed on the various role-players in terms of the Financial Markets Act.

### 2.2 Exchanges

#### 2.2.1 Licensing of an exchange

Any person (including a company and an association of persons) may apply for an exchange license in respect of one or more types of security.

The application must be in such format and be accompanied by such documents as determined by the Commissioner of the FSCA.

In the past, only an association of persons could apply. These new provisions enable an exchange to become “demutualized” i.e., to become a company and even list on its own exchange. This is the trend internationally as well.

The JSE Ltd has listed on its own exchange in terms of conditions laid down by the Commissioner. The regulatory functions of the exchange regarding its own listed securities are taken over by the Commissioner.

Different types of exchanges with different business models, such as traditional exchanges, electronic communications networks and alternative trading systems may be granted a license, as the Commissioner may determine to what extent compliance with the requirements must take place.

The requirements for an exchange license include the following:

- An applicant must have adequate financial resources, management and human resources with the necessary experience and the necessary infrastructure to conduct an exchange.
- All transactions must be supervised through surveillance systems to ensure compliance with exchange rules.
- The integrity of records must be safeguarded through security back-up procedures.
- Adequate clearing and settlement facilities and the proper management of settlement risk must be provided for.
- Compensation to clients must be ensured by insurance, a guarantee or compensation fund or some other warranty.

The Commissioner will issue an exchange license only if the requirements have been complied with to the extent decided by the Commissioner and the issuance of the license will promote the objects of the Act.

It follows that if the issue of an exchange license may for example lead to systemic risk, the Commissioner will refuse the license even if the applicant complies with the requirements.

The license of an exchange expires on 31 December of every year. Application for renewal must be made in the manner determined by the Commissioner.

### **2.2.2 Funding of an exchange**

An exchange may require its authorised users and their clients to contribute towards the funds of the exchange for purposes of conducting the business of an exchange.

A surplus that may arise may be distributed to any person if proper provision has been made for liabilities, the distribution is made in accordance with its founding document and the prior written consent of the Commissioner has been obtained.

An exchange may impose a transaction levy to maintain the insurance, guarantee or compensation fund or other warranty that an exchange must have in place for the protection of investors making use of its trading facilities.

### **2.2.3 Management and control of an exchange or other SRO**

Each member of a controlling body of an exchange owes a fiduciary duty to the exchange. This means that the members must act with the utmost good faith towards the exchange and always put the interests of the exchange first. In addition, they owe a duty of care and skill towards the exchange. If the SRO is a company, a member will be a director and the controlling body the board of directors.

No person who is precluded from becoming a director of a company in terms of the Companies Act may be appointed as a member of the controlling body. The same applies to anyone penalized for the contravention of the rules of a professional organisation, including an SRO.

No person may without the Commissioner's approval acquire shares or other interest in an exchange or other SRO if the acquisition will enable such a person directly or indirectly and with or without an associate to exercise control over an exchange or SRO.

Exercising control means holding shares in an exchange or other SRO that exceeds 15% of the nominal value of issued shares or 15% of the voting rights without the approval of the Commissioner. In addition, no person may have the power to determine the appointment or removal of 15% or more of the directors of the exchange or other SRO without the approval of the Commissioner.

These provisions ensure that disreputable persons do not seize control of an exchange or other SRO and thereby introducing systemic risk into the securities markets.

### **2.2.4 General functions of an exchange**

An exchange provides the infrastructure for bringing together buyers and sellers of those securities in respect of which a license has been obtained and matching those orders to buy or sell. Once matched, the orders become transactions.

The exchange must also provide for the clearing and settlement of transactions. A licensed clearing house may be used for these purposes. In South Africa STRATE Ltd is licensed as a clearing house in addition to its function as a Central Securities Depository (CSD). All the exchanges make use of STRATE Ltd's clearing services except for the derivatives market, which uses SAFCOM.

The FMA confers the status of an SRO on an exchange and imposes regulatory duties and functions on the exchange for example:

- Issuing directives in terms of its rules (directives contains internal procedures that do not affect clients).
- Enforcing the exchange's rules and listing requirements.

- Supervising compliance by authorised users with the Act and the rules.
- Supervising compliance by issuers with the Act, rules and listing requirements.
- Amending or suspending the rules and listing requirements.

These duties are performed under the supervision of the Commissioner. If the Commissioner deems it necessary to achieve the objects of the FMA Act, the Commissioner may take over these functions.

### **2.2.5 Listing of securities**

An exchange must keep a list of securities that may be traded on the exchange. Issuers will apply to the exchange for the listing of their securities.

Such securities must comply with the listing requirements of the exchange, which must prescribe the following:

- The way securities will be listed, suspended or removed from the list.
- The requirements that issuers and their agents must comply with.
- The standards of conduct that issuers, their agents, directors and officers must comply with.
- The standards of disclosure and corporate governance that issuers must comply with.
- The disciplinary procedure in respect of the contravention of listing requirements, including the penalties that may be imposed.

An exchange may also impose conditions in respect of the listing when approving an application for the listing of a security.

Provision may be made in the listing requirements that details regarding the imposition of a penalty may be published. The person guilty of a contravention may be ordered to pay the costs of the investigation.

The exchange may list its own securities subject to the approval of the Commissioner and compliance with such conditions as the Commissioner may determine.

In this instance, the exchange is thus both the issuer and the exchange. This clearly constitutes a conflict of interest as the exchange's objectivity in considering the listing is compromised. For that reason, the Commissioner will retain the right to approve the listing and will take over the exchange's regulatory functions regarding its own listed securities.

An exchange must, before refusing a listing application, inform the issuer of its decision giving reasons for the refusal. The issuer must be given the opportunity within a stated period to provide reasons why the application should not be refused.

### **2.2.6 Removals and suspensions**

The exchange may remove a security from the list of securities or suspend trading in a security if such removal would promote the objects of the Act.

An exchange must before removing a security from the list or suspend trading, inform the issuer of its decision giving reasons for the removal or suspension. The issuer must be given the opportunity within a stated period to provide reasons why the security should not be removed from the list or suspended.

An exchange may order an immediate suspension of a listed security for a period not exceeding 30 days if the listing requirements, conditions or rules are contravened or other circumstances arise that justify an immediate suspension of the security. This period may be extended for further periods of 30 days by the exchange.

Trades in suspended securities on the exchange will only be allowed to fulfill obligations acquired before the suspension.

An issuer requesting removal of its securities from the list, may only do so provided the holders of its securities have approved the removal and the exchange is satisfied that the interests of minority shareholders have been considered. The issuer must under these circumstances also provide reasons for its request.

An exchange refusing the listing of a security or suspending or removing a security must immediately inform other exchanges on which the security is listed thereof and provide the date of and reasons for the refusal, suspension or removal.

If the refusal to list or removal from the list was due to any fraud or crime committed by the issuer, or material misstatement of its financial position or non-disclosure of any material fact, or to a failure to comply with listing requirements, no other exchange may within 6 months thereafter list the security or allow trade unless the refusal or removal was withdrawn or set aside on appeal.

### **2.2.7 New listing requirements**

An exchange may also impose new listing requirements or conditions on existing listed securities by notice in writing to the issuer.

The new listing requirements or conditions will take effect on a date determined by the exchange but not earlier than 1 month after the notice to the issuer, except when special circumstances justify an earlier date.

The exchange may postpone the date on written request from the issuer. If the exchange refuses a request for postponement, the issuer may make representations to the Commissioner, who may, if reasonable and after consultation with the exchange, postpone the date by not more than 3 months.

### **2.2.8 Disclosure of information by issuers**

An exchange may require an issuer to disclose any information about the securities or the affairs of the issuer that may be necessary to achieve the objects of the Act.

The exchange may also require disclosure of the information to the holders of the securities within a specified period.

If such disclosure may affect the price of the securities, disclosure must be made at the same time to the public. If the issuer refuses to make the necessary disclosure, trade in that security may be suspended unless a court order has been obtained to allow non-disclosure.

### **2.2.9 The rules of the exchange**

An exchange must make rules to govern their activities and operations. The Commissioner must approve the rules. The rules will be binding on the exchange, authorised users, issuers, officers and employees and clients and must be consistent with the Act.

The rules must make provision for the following aspects: -

- The criteria for authorisation of authorised users. These criteria must include the following:
  - Requirements that authorised users must be of good character and high business integrity or in the case of a corporate entity be managed by such persons.
  - Requirements that authorised users comply with certain standards of training, experience or qualifications or in the case of a corporate entity, is managed by such persons or employs such persons.
  - Requirements in respect of capital adequacy, guarantee or risk management. These requirements must be prudent but may differ among different categories of authorised users or different activities of an authorised user's business.
  - Restriction of the activities of different categories of authorised users.
- The efficient, honest, transparent or fair way transactions must be made whether for own account or for clients.
- The clearing and settlement of transactions, including when a licensed clearing house has not been appointed.

- The circumstances under which transactions may be repudiated or declared void.
- The conditions on which an authorised user may undertake the management of investments.
- A requirement that no authorised user may accept business from unapproved financial services providers e.g., investment managers.
- The approval of nominees holding securities in a securities or central securities depository.
- The conditions subject to which officers and employees of authorised users may advise on or conclude transactions and when access to the exchange may be denied.
- The suspension or halting of trade in a listed security.
- The way authorised users must conduct their business generally, including the operation of a trust account, the recording of transactions, monitoring of compliance and surveillance of activities relevant for the Act, the rules or directives and the circumstances and the way an authorised user may advertise or canvass for business.
- The resolution of disputes between authorised users and between authorised users and their clients and the investigation of complaints against authorised users or their employees.
- The investigation and disciplining of authorised users or their employees for contravention of the Act, rules or directives, including the way an authorised user or its employee may be required to appear before an investigator to be interrogated or to produce a document. A report of the proceedings must be provided to the Commissioner within 30 days thereafter.
- Persons who must contribute to the insurance or guarantee or compensation fund, the amount of the levy, the different categories of claims and the restrictions thereon, the administration and the ownership of the fund.
- The different categories of transactions will attract different fees and the disclosure of fees to clients.
- The purpose for which directives may be issued.
- Supervision of compliance with the Financial Intelligence Centre Act (FICA).
- The supervision by an exchange with the duties imposed by the Financial Intelligence Centre Act, the reporting of any non-compliance of these duties to the registrar and the assistance to be provided to the registrar on enforcing the Act.

## 2.3 Authorised users

An authorised user is a person (including a company and any other juristic entity) that has been authorised by the exchange to render securities services.

Previously authorised users were known as members of the exchange.

An authorised user will only be authorised by the exchange if it:

- Is of good character and high business integrity or in the case of a corporate entity is managed by such persons.
- Complies with certain standards of training, experience or qualifications or in the case of a corporate entity is managed by such persons or employs such persons.

An authorised user must comply with the requirements in respect of capital adequacy, guarantee and risk management as prescribed in the rules.

### 2.3.1 Segregation of funds and assets

Each authorised user must, in respect of clients' money, open a separate trust account at a bank or utilise the separate trust account opened by the exchange. These accounts may contain client funds only.

An authorised user must deposit the payment on the day of receipt of payment from a client. If payment was received after hours or was made directly into the authorised user account, it must be transferred to the authorised user's trust account by the start of business the following day.

An authorised user does not have to make a deposit in the following circumstances:

- If payment is made by the buyer against delivery of the securities.
- If payment is made by the buyer against such securities being marked or recorded as the property of the buyer.
- If the payment is preceded by a payment made by the authorised user to a seller against delivery of the securities to the authorised user.
- If the payment is made to pay a debt due to the authorised user. Debt arising from the purchase of listed securities which have not been marked as the property of a buyer will not be regarded as a debt.
- If the payment is made in terms of any other law or exchange rule which specifically provides for the payment to be made into some other account.

The following funds constitute trust property:

- Funds held in a trust account.
- Funds not deposited in a trust account but identifiable as belonging to a specific person.

Withdrawal from a trust account may only take place under the following circumstances:

- To pay the person entitled to the payment
- To pay in terms of any other law or the rules.

If a cheque, draft or other instrument deposited in the trust account is dishonored after the withdrawal, the authorised user must immediately pay the shortfall into the trust account.

Bank charges in respect of a trust account are for the account of the authorised user except bank charges in respect of a deposit or withdrawal of a specific person's funds, in which case they will be for that person's account.

Interest accruing on a trust account is due to the person entitled to the funds after payment of fees due to the authorised user or exchange.

The excess remaining in the trust account after payment of or provision for all claims of persons whose funds have or should have been deposited in the account shall NOT be trust property.

### **2.3.2 Marking of or recording details of securities**

When a document of title comes into possession of the authorised user, it must be marked and recorded, and the necessary details stored so that the owner can be readily identified.

### **2.3.3 Restriction on borrowing, re-pledging and alienation**

An authorised user may not borrow against pledged securities in an amount exceeding the outstanding balance of any amount that the authorised user may have lent the pledgor against the pledged securities. An authorised user may also not re-pledge listed securities without the consent of the pledgor.

An authorised user may only alienate (sell) listed securities deposited with the authorised user if the depositor has authorised it in writing.

### 2.3.4 Code of conduct

The Commissioner may prescribe a code of conduct for authorised users, participants or clearing members of independent clearing houses.

The Commissioner may also prescribe a code of conduct for any other regulated person in respect of which the required standard of conduct is not prescribed in another law or code of conduct and a code of conduct is necessary or expedient for the achievement of the objects of the FMA. Consultation of the relevant industry must take place prior to such code becoming law.

The code of conduct will be binding on the authorised users, participants, clearing members of independent clearing houses or other regulated persons as well as their officers, employees and clients.

A code for authorised users, participants, clearing members of independent clearing houses must be based on the principle that it must-

- Act honestly and fairly and with due skill, care and diligence and in the interests of the client.
- Uphold the integrity of the financial markets.
- Have and effectively employ the resources, procedures and technological systems for the conduct of its business.

In the case of authorised users, the code must also provide that it must-

- Seek information from a client about his or her financial position, investment experience and objectives where appropriate to the category of securities services provided and to the business of the client.
- Act fairly in a situation of conflicting interests.

The code of conduct for a regulated person other than the above (such as exchanges, CSDs etc.) must be based on the principle that it must-

- Act honestly and fairly and with due skill, care and diligence and, where applicable, in the interests of the client or member.
- Uphold the integrity of the financial markets.

In addition, a code of conduct may provide for-

- Disclosure to a client of relevant material information, including the disclosure of actual or potential own interests.
- Proper record-keeping.
- Avoidance of fraudulent and misleading advertising, canvassing and marketing.
- Proper safekeeping of clients' transaction documents.
- Proper separation and protection of clients' funds and securities.
- Any other matter necessary or expedient to be regulated in a code of conduct for the achievement of the objects of the FMA.

### **2.3.5 Cessation of business of an authorised user**

An authorised user or participant that ceases business must attend to the following:

- Notify the exchange or central securities depository of the intended or actual date of cessation of business.
- Notify the clients for whom they hold assets or funds, in writing, of the intended or actual date of cessation of business, provide those clients with statements reflecting the assets and funds held on their behalf and indicate to which authorised user, participant or other person authorised to deal in or hold custody of securities their assets and funds will be delivered in the absence of an instruction from the client to the contrary.
- Deliver the client assets and funds.

An authorised user that ceases business must maintain a record of funds or assets held in trust until the transfer to a client or another person authorised to deal in or hold custody of securities has been fully affected.

### **2.3.6 Accounting records**

A regulated person must maintain on a continual basis accounting records and prepare annual financial statements that conform to generally accepted accounting practice (GAAP) and contain the information prescribed by the Commissioner.

The financial statements must be audited within 3 months after the financial year-end or such later period as the Commissioner may allow.

Accounts of clients must be designated as such and must be clearly distinguishable from the business accounts of a regulated person. A regulated person may keep computerized records provided that such records are subject to acceptable backup and recovery procedures and can be reproduced in printed form.

An authorised user, participant or clearing member of an independent clearing house must keep the following accounting records regarding securities services rendered:

- A daily record of all sums of money received and expended.
- A record of funds held in trust.
- A record of all income and expenditure.
- A record of all assets and liabilities, including any provisions for financial commitments and contingent liabilities.
  - A record of all purchases and sales of securities which reflects the following:
    - Date and time of each transaction.
    - Person from whom securities were bought or to whom they were sold, unless it was processed through an automated trading system recognised by the relevant exchange.
    - Name of the person on whose behalf the securities were bought or sold.
    - Quantity and description of the securities which were bought or sold.
    - Name of the issuer of the securities.
    - Price per security and the total consideration.
    - Fees and charges.
    - Taxes that are payable in respect of each transaction
    - Terms of the contract
    - Capacity (principal or agent) in which the transaction was entered into
    - The following additional information in respect of transactions in options:
      - The reference number of the transaction and option number, where applicable.
      - Whether the option is a put or call option.
      - The terms and conditions under which the option may be exercised, including the type of option, the strike price or yield, the strike date and time and the settlement date.
      - The identity of the writer of the option.
      - The quantity and description of the listed security to which the option relates.

- The option premium and settlement date.
  - Whether the option was exercised or lapsed and the exercise date, if applicable.
- A record of all securities and documents of title which are in the possession, safe custody or under its control in which the following is reflected:
  - Name of the issuer of the securities.
  - Quantity and description of the securities.
  - Identification numbers of the securities and documents of title, where applicable.
  - Name of the registered holder and if the registered holder is a nominee controlled by the regulated person, the name of the person on whose behalf the nominee is holding the securities.
  - Person from whom the securities were received and to whom the securities were delivered.
  - Date of receipt and delivery.
  - Location where the securities or documents of title are kept.
  - Details of any pledge to which the securities may be subject.
  - Person on whose behalf securities or documents of title have been received or delivered.
  - Purpose for which the securities or documents of title are held.
- A record of securities held by the authorised user on behalf of its clients which must be made available to its clients as frequently as required in terms of the applicable rules or directives and which must contain as a minimum the following:
  - The name of the client.
  - The quantity and a description of securities held.
  - A description of transaction movements within the securities accounts during the period since the previous report.
- A record of the reconciliation of the securities accounts maintained by a participant and the central securities account maintained by the central securities depository.

An authorised user, participant or clearing members must reconcile balances with the exchanges, clearing houses, central securities depositories, participants and banks if applicable, as frequently as required in terms of applicable rules or directives for the volume of transactions on accounts.

Any differences, other than differences in timing between the records must be investigated immediately and corrected as soon as required in terms of the applicable rules or directives.

Authorised users must reconcile securities under their control with the accounting records relating to securities held by the authorised user daily. Correcting entries must be done immediately.

The accounting records (which may be electronic) must be preserved in a safe place for at least five years from the date of the last entry.

## **2.4 Auditors**

Every regulated person must appoint an auditor who engages in public practice. The auditor must be independent.

No auditor or member of an auditor firm in which a regulated person or director, officer or employee of a regulated person has any financial interest, may be appointed as auditor.

The appointment of an auditor by an SRO must be approved by the Commissioner who may also withdraw the approval if necessary.

The appointment of an auditor by a market infrastructure (i.e., an exchange, clearing house or central securities depository) must be approved by the Commissioner who may also withdraw the approval if necessary.

The auditor must audit the annual financial statements of a regulated person in accordance with the International Financial Reporting Standards to ascertain the following:

- Whether the financial statements are in accordance with the underlying records.
- Whether the financial statements have been prepared in accordance with the above said Standards, the Companies Act and the FMA.
- Whether the financial statements fairly present the financial position, cash-flows and the results of the operations of the regulated person.

The auditor of an authorised user must report to the exchange (as SRO) (or to the FSCA at the Commissioner's request) that the accounting records and the annual financial statements have been examined in accordance with Generally Accepted Accounting Principles (GAAP) and that they fairly present the financial position, cash flows and results of operations.

The report must also include the following:

- Whether or not securities that have been entrusted to the regulated person or for which the regulated person is accountable, are in the possession of the regulated person or a custodian, and whether confirmations or statements of holdings have been obtained from the persons who maintain the record of ownership of such securities.
- Whether the authorised user complied with the FMA regarding the operation and maintenance of its trust account.
- Whether the authorised user complied with the capital adequacy requirements determined by the rules of the exchange.

#### **2.4.1 Responsibility of Auditor upon cessation of business of an authorised user**

The auditor of a regulated person must report, within 3 months of the date on which the regulated person ceased to do business, on whether the regulated person has complied with the record keeping requirements upon cessation of business.

## **2.5 Custody and Administration of Securities**

### **2.5.1 Registration and transfer of securities**

The Companies Act makes provision for securities issued by a company to be either evidenced by a certificate (i.e., to be certificated) or to be uncertificated.

Every company must establish and maintain a register of issued securities in accordance with prescribed forms and standards.

An issuer of uncertificated securities (e.g., a company issuing uncertificated shares) must record in its securities register the total number of securities and where applicable, the nominal value of each kind of uncertificated security issued by it.

If the company issued certificated securities, it must also enter the following:

- The names and addresses of the persons to whom the securities were issued, and the number of securities issued to them.
- The number of and circumstances of securities that have been placed in trust or whose transfer has been restricted.
- The number of debt instruments issued and outstanding or the names and addresses of the registered owners and holders of beneficial interest.
- Any other prescribed information.

If the company issued uncertificated securities, a record must be administered and maintained by a participant or central securities depository as the company's uncertificated securities register. This register forms part of the company's securities register. This register must contain the same information referred to above or the details determined by the rules of the central securities depository.

Transfer of ownership takes place upon the debiting and crediting, respectively, of the account in the uncertificated securities register from which the transfer is made and the uncertificated securities register to which transfer is made in terms of the rules of a central securities depository.

Only a participant or central securities depository may affect such a transfer on receipt of an instruction to transfer sent and authenticated in terms of the rules of the central securities depository or an order of court.

### **2.5.2 Custody of securities**

The FMA makes provision for the safe custody and record keeping of securities by central securities depository (CSD) and participants of the CSD.

A central securities depository provides an infrastructure for holding uncertificated securities in respect of which entries to be made. Such an infrastructure must include a securities settlement system.

A participant in a CSD is a person (usually a bank) authorised by a licensed central securities depository to perform custody or administration services or both.

A CSD must be licensed by the FSCA, like the approach followed with respect to the exchanges. A CSD operates in terms of its rules that must be approved by the FSCA.

Where securities are deposited with a participant or CSD, the owner of the securities becomes entitled to an interest as co-owner of all the securities of the same kind comprised in the securities account or central securities account.

The interest of a co-owner is calculated by reference to the proportion that the number or nominal value of the securities deposited bears to the total number or nominal value of the securities of that kind held in the securities account or central securities account.

A written statement issued by or on behalf of a participant or central securities depository and specifying the interest of that owner is sufficient proof of the title in such securities.

Securities held by a central securities depository, participant or nominee for another person must be segregated and identifiable as belonging to a specific person and are deemed to be trust property as defined in the Financial Institutions (Protection of Funds) Act.

Every person depositing securities with a participant or CSD is deemed to warrant that such person is entitled to deposit the securities and that the document or instruction is genuine and correct.

Such person is also deemed to indemnify the participant or central securities depository for any loss incurred out of such loss or warranty. A CSD is, however, not deemed to have given such an indemnity or warrant.

### **2.5.3 Duties and Functions of a CSD**

A Central Securities Depository (CSD) must conduct its business in a fair and transparent manner with due regard to the rights of participants, their clients and issuers. It must provide an infrastructure for holding uncertificated securities in respect of which entries to be made.

Such an infrastructure must include a securities settlement system. It must also provide custody and administration in respect of a central securities account.

A CSD must issue depository rules, which may be amended or suspended. Directives may be issued if necessary. It has a duty to enforce both.

A CSD must also supervise compliance by participants with the rules and directives and by participants with the FMA. Non-compliance must be reported to the Commissioner and assistance must be provided to the Commissioner with enforcing the FMA.

The Commissioner must be informed of any matter that may pose systemic risk to the financial markets in the opinion of the CSD.

A CSD must maintain a central securities account with due regard to the interests of the participant and its clients. A central securities account refers to an account kept by the CSD for a participant or external central securities depository that reflects the number or nominal value of securities of each kind deposited and all entries made in respect thereof.

A CSD must administer and maintain a record of all uncertificated securities deposited with it.

All securities of the same kind deposited by a participant may be held collectively in a separate central securities account.

A CSD may have access to the records of uncertificated securities administered and maintained by its participants.

A participant must be notified in writing of all entries made in the participants' central securities account. Entries include an electronic recording of any issuance, deposit, withdrawal, transfer, attachment, pledge, cession to secure a debt or other instruction in respect of securities.

The aggregate of the central securities accounts and the records of the relevant issuer must be reconciled and balanced in respect of each kind of certificated security at least every six months and in respect of uncertificated securities not less than once a month if the aggregate has not changed and if the aggregate has changed, on the business day after the change.

A CSD must on request disclose to the Commissioner information about the securities held in the central securities account.

It must also on request disclose to an issuer information about the securities issued by that issuer and held in central securities accounts.

A CSD may clear transactions if it has been granted a clearing house license.

Fees and charges must be disclosed to persons for whom central securities accounts are kept, participants and issuers. The disclosure must give the specific monetary amount for each service rendered or if such amount is not pre-determinable, the basis of the calculation.

If a participant ceases to be a participant, the Commissioner must be notified.

A CSD may enter into an agreement with an external securities depository for the provision of securities services.

STRATE Ltd is currently the only licensed CSD in South Africa.

#### **2.5.4 Duties and functions of a participant**

A participant must conduct its business in a fair and transparent manner with due regard to the rights of its clients.

A participant must deposit securities deposited with it with a licensed central securities depository. It must maintain a securities account for each client in respect of securities deposited.

A securities account reflects the number or nominal value of securities of each kind deposited and all entries made in respect of such securities. A record of all securities deposited must be administered and maintained in accordance with the rules of the CSD. All the securities of the same kind must be recorded in an uncertificated securities register if so, required by the rules of the CSD.

Fees and charges must be disclosed to clients and issuers. The disclosure must give the specific monetary amount for each service rendered or if such amount is not pre-determinable, the basis of the calculation.

If an entry is made in the client's securities account, the client must be notified in writing or as otherwise agreed.

A participant must on request disclose to the Commissioner information about the securities recorded in a securities account. The participant must also on request disclose to the issuer information about the securities issued by that issuer and recorded in a securities account.

A participant must have a central securities account with a central securities depository in which it may deposit or withdraw securities.

A participant may also transfer, attach, pledge, cede or give effect to any other lawful instruction in respect of a security or an interest in securities through that central securities depository. It must exercise the rights in respect of securities deposited by it with the central securities depository in its own name on behalf of the client if instructed to do so.

A participant must balance and reconcile the aggregate of the securities accounts with the central securities accounts daily.

### **2.5.5 Nominees**

The FMA provides for the approval of nominees that act as the registered holders of securities or an interest in securities on behalf of others.

A nominee of an authorised user must be approved in terms of the rules of the exchange. A nominee of a participant or the nominee of a client of the participant must be approved by the CSD in terms of the depository rules.

Other nominees must be approved by the Commissioner and comply with requirements prescribed by the Commissioner. The Commissioner must maintain a list of approved nominees.

## 2.6 Clearing

### 2.6.1 Duties and functions of a clearing house

Clearing houses must be licensed by the Commissioner to fulfil the function of clearing of transactions. The function of a clearing house is to calculate and determine before each settlement process the exact number of nominal values of each kind to be transferred by or on behalf of a seller and the amount of money to be paid by the buyer to enable settlement of the transactions or group of transactions.

A clearing house must conduct its business in a fair and transparent manner with due regard to the rights of clearing members and their clients.

The clearing house must provide an infrastructure for the clearing of securities through the clearing house and manage the clearing of transactions accepted for clearing and if licensed to do so, the settlement of those transactions. It must have appropriate arrangements in place to ensure that it has efficient and timely access to funds and assets held as collateral for the due performance of the obligations of clearing members and to protect the funds and collateral of clearing members in case a clearing member defaults.

The Commissioner must be informed of any matter that may pose systemic risk to the financial markets in the opinion of the clearing house. It must also upon request disclose to the Commissioner information on the exposures that a clearing member underwrites with the clearing house.

A clearing house must issue and enforce clearing house rules and may also amend or suspend them. It may issue directives if deemed necessary.

The clearing house must also supervise compliance by its clearing members with the rules and directives as well as the FMA. In case of non-compliance with the FMA, it must report it to the Commissioner and assist the Commissioner with enforcement.

Different rules for clearing and settlement of different securities and clearing members may be made. When making or amending rules, a clearing house must consult relevant regulated persons i.e., an exchange, authorised user, CSD, participant, clearing member, nominee and trade repository.

Fees and charges must be disclosed to clearing members. The disclosure must give the specific monetary amount for each service rendered or if such amount is not pre-determinable, the basis of the calculation.

If a clearing member ceases to be a clearing member, the clearing house must notify the Commissioner.

## **2.7 Duties and functions of a trade repository**

A trade repository is a person who maintains a centralized electronic database of transaction data and must be licensed by the Commissioner.

It must conduct its business in a fair and transparent manner. It must employ timely, efficient and accurate record keeping procedures.

Such information as the Commissioner may prescribe must be made available to the Commissioner, other supervisory authorities and other persons in accordance with the Commissioner's requirements.

These requirements may pertain to form, manner and frequency of disclosure. The trade repository must ensure the confidentiality, integrity and protection of the information. It must also make such information available to the Commissioner as may be requested for purposes of monitoring and mitigating systemic risk.

It must monitor and evaluate the adequacy and effectiveness of its systems, internal control mechanisms and arrangements and take appropriate measures to address any deficiencies.

Fees and prices for services must be publicly disclosed. Such disclosure must give the specific monetary amount for each service rendered or if such amount is not pre-determinable, the basis of the calculation.

## TOPIC 3 UNLAWFUL BEHAVIOUR IN THE FINANCIAL MARKETS

### LEARNING OUTCOMES

After studying the topic, the learner should be able to-

- Identify whether an offence of insider trading has been committed.
- Name the trading practices that the Financial Markets Act prohibits.
- Understand the stipulations regarding False, misleading or deceptive statements, promises and forecasts.
- Outline the powers of the Directorate of Market Abuse.

### 3.1 Introduction

Any unlawful behavior in the financial markets is prohibited. The concept of market abuse typically consists of insider dealing, unlawful disclosure of inside information, and market manipulation.

### 3.2 Insider Trading

The offence of insider trading has been committed if the elements 1, 2 and 3 of the table below in any combination are present.

#### 1. The Insider (The person)

- A director, employee or shareholder of an issuer of securities to which the inside information relates.
- An individual who has access to inside information by virtue of his or her employment, office or profession.
- An individual who knows that the direct or indirect source of the inside information was one of the two persons above.

## **2. The Offence (The activity)**

- Dealing directly or indirectly for own account or for any other person (knowing that he or she has inside information) in securities listed on a regulated exchange to which the information relates or that are likely to be affected thereby.
- Disclosing inside information to another person.
- Encouraging or causing another person to deal or discouraging or stopping another person from dealing in securities listed on a regulated market to which the information relates or that are likely to be affected thereby.

## **3. The Inside Information**

Specific or precise information: -

- That has not been made public
- That has been obtained or learned as an insider and If made public is likely to have a material effect on the price or value of any security listed on a regulated market.

Made public includes:

- Publishing information by a regulated market to inform clients and professional advisers.
- When information is contained in records open to inspection by the public.
- When the information can easily be obtained by those likely to trade in listed securities to which the information relates or to the issuer of those securities.

Information will still be regarded as public even though –

- It can only be acquired by persons exercising diligence and observation.
- It can only be obtained on payment of a fee.
- Was published outside of SA.

### 3.2.1 Defenses to Insider Trading

A person will however NOT be found guilty of the offence in the following circumstances and these circumstances may therefore be raised as a defense:

- If he or she acted on the specific instructions of a client. (Except where the client disclosed the insider information to him or her).
- If he or she became an insider after he or she had given the instruction to deal to an authorised user and the instruction was not changed in any way.
- If he or she acted on behalf of the public sector in the pursuit of certain government policies.
- If he or she was acting in pursuit of a take-over or merger.
- If he or she disclosed inside information because it was necessary for the proper performance of the functions of his or her employment, office or profession in circumstances unrelated to dealing in any security listed on a regulated market and at the same time disclosed that the information was inside information.

### 3.2.2 Civil Liability in respect of Insider Trading Offences

A person who knows that he or she has inside information and makes a profit or would have made a profit if the securities were sold at any stage or avoided a loss through a direct or indirect insider trade (the insider trader), shall be liable to pay to the Financial Services Board the following amounts:

- The amount of the profit or loss referred to above.
- A compensatory or punitive amount determined by the Court but not exceeding three times the above-mentioned profit or loss.
- Interest.
- The costs of the suit.

A person who knows that he or she has inside information who discloses the inside information to the insider trader, encourages the insider trader to trade on the inside information or trades directly or indirectly on behalf of the insider trader (like a stockbroker), shall be jointly and severally (*i.e., he or she can be held liable in lieu of the insider trader*) liable with the insider trader for the above-mentioned amounts as well as the commission or other consideration received.

### 3.3 Prohibited Trading Practices

Knowingly using or participating in manipulative, improper, false or deceptive trading practices in listed securities that may create a false or deceptive appearance of trading or an artificial price for that security is an offence.

Placing an order that may create a false or deceptive appearance of trading or an artificial price for that security is also an offence. This applies regardless whether trading took place directly or indirectly, for own account or behalf of someone else.

The following will be deemed to be manipulative, improper, false or deceptive trading:

- Approving or entering an order to buy or sell a security without a change in beneficial ownership.
- Approving or entering an order to buy or sell a security with the knowledge that an opposite order/s of substantially the same size, at substantially the same time and price with the intention of creating a false or deceptive appearance of trading or an artificial price for that security.
- Approving or entering orders to buy a listed security at successively higher prices or orders to sell at successively lower prices to unduly or improperly influencing the market price of such a security.
- Approving or entering an order to buy or sell a security at or near the close of the market, the purpose of which is to change or maintain the closing price of a security.
- Approving or entering an order to buy or sell a security listed on that market during any auctioning process or pre-opening session and cancelling that order immediately prior to the market opening for creating a false or deceptive appearance of demand or supply for such security.
- Effecting or assisting in effecting a market corner. A market corner is where a person or group of persons acting together have an arrangement, agreement, commitment or understanding to acquire direct or indirect beneficial ownership of or exercising control over or is able to influence the price of listed securities and where the effect thereof is that the trading price reflected on the exchange is likely to be abnormally influenced or arbitrarily dictated by such a person or group of persons in that the trading price deviates materially or is likely to deviate materially from the trading price that would otherwise have been reflected.
- Maintaining the price for dealing in listed securities at an artificial level.
- Employing any device, scheme or artifice to defraud any other person because of a transaction effected through the exchange.

- Engaging in any act, practice or course of business in respect of dealings on the exchange, which is deceptive or is likely to be deceptive.

**BUT NOT** the employment of price-stabilising mechanisms regulated in terms of the rules or listing requirements of an exchange.

### **3.4 False, misleading or deceptive statements, promises and forecasts**

No one may make or publish a false, misleading or deceptive statement, promise or forecast regarding a material fact concerning listed securities or the past or future performance of a public company while he or she knows or ought to have known that it is false, misleading or deceptive.

The same applies to an omission of facts having the same effect. Such an action will be a criminal offence.

When considering whether the offence took place, it will be evaluated in the light of the circumstances prevalent when it took place.

### **3.5 Directorate of Market Abuse**

The Directorate of Market Abuse exercises the powers granted to the FSCA regarding investigating and instituting proceedings regarding insider trading, prohibited market practices, and publishing of false, misleading or deceptive statements.

These powers relate to offences that took place on a regulated market in South Africa as well as similar offences that may have taken place according to the laws of another country if so, requested by a supervisory authority of that country.

The Directorate of Market Abuse may after an investigation refer an alleged contravention to the Enforcement Committee.

Investigative powers of the FSCA that may be exercised by the Directorate of Market Abuse briefly include the following:

- Summoning a person with information or documents to appear for interrogation or to produce documents.
- Interrogate such a person under oath or affirmation and examine the document or retain the document for examination.
- On the authority of a warrant, without prior notice, or subject to the consent of the person in control of the premises do the following:

- Enter any premises and require the production of any document.
- Enter and search any premises for any document.
- Open any strong room, safe or other container.
- Examine, make extracts from and copy any document or against the issue of a receipt, remove such document temporarily
- Against the issue of a receipt, seize any document.
- Retain any seized document for as long as it may be required for criminal or other proceedings.

A failure to appear, furnish information or provide a document on the part of the above-mentioned person constitutes an offence and is liable on conviction to a fine or imprisonment not exceeding two years or to both the fine and imprisonment.

Any entry or search of the premises must be conducted with strict regard to decency and good order including a person's right to, respect for and the protection of dignity and the right of a person to freedom, security and personal privacy.

The Minister must appoint the members of the Directorate which must include the executive officer of the FSCA or his deputy or both, and persons with appropriate experience and an alternate from the following professions: a commercial lawyer, an accountant, a person from the insurance industry, a person from the banking industry, a person from the fund management industry, a person from any organisation representing shareholders' rights and a person nominated by the SA Reserve Bank. An additional two members with appropriate knowledge of financial markets and experience must be appointed.

Members of the Directorate may not be practising authorised users.

### **3.5.1 Other powers of the FSCA regarding market abuse offences**

The Financial Sector Conduct Authority (FSCA) may apply to court regarding any market abuse matter for an interdict or an order to attach assets or evidence to prevent the concealment, removal, dissipation or destruction.

The FSCA may publish on their website or other media the outcome of any investigation and details of the investigation of disclosure in the public interest.

The FSCA may make market abuse rules after consultation with the Directorate of Market Abuse regarding:

- Administration matters.
- The way investigations are to be conducted.
- Notifications regarding amounts received because of administrative sanctions and the procedure for the lodging and proof of claims, the administration of trust accounts and the distribution of payments in respect of claims.
- Meetings of the Directorate.
- The way inside information should be disclosed.
- The conduct of a person relating to inside information.

The FSCA may, after consultation with the regulated markets in South Africa, require the markets to implement such systems as may be necessary for the monitoring or identification of market abuse practices.