

FINANCE AND BANKING ALERT

IN THIS ISSUE

ELECTRONIC FLAGGING UNDER THE CONSOLIDATED STRATE RULES

In line with s39(3) of the FMA, Strate has now proposed a so-called "wheelbarrow" pledge rule in respect of "Securities Accounts" held in Strate. The "Securities Account" itself may now be pledged or ceded *in securitatem debiti* to the pledgee or cessionary as security for any existing monetary obligations of the pledgor or cedent. The "Securities Account" (and all of the Securities standing to the credit of such an account at the time that the pledge is effected) may now be electronically flagged in favour of a pledgee or cessionary as an alternative to electronically flagging specific Securities held in a "Securities Account".

TACIT FAIS ADVICE

You walk into a cellphone shop with the intention of buying a new mobile phone and, on completion of the transaction, the salesperson asks you whether you want insurance cover for your new device. You say yes, so he hands you the insurance documents and points to a clause containing the calculation of your monthly instalment. You're happy and he shows you where to sign, which you do. But... did the salesperson in this scenario provide 'advice' in terms of the Financial Advisory and Intermediary Service Act (FAIS) and therefore should the salesperson comply with FAIS?

ELECTRONIC FLAGGING UNDER THE CONSOLIDATED STRATE RULES

FMA states that an interest in respect of uncertificated Securities may be granted in the manner provided for in the Strate Rules, where such an interest extends to all uncertificated Securities standing to the credit of the "Securities Account" at the time the pledge is effected.

CSDPs are required to send statements to the pledgee or cessionary evidencing the existence of the pledge or cession in securitatem debiti over specifically flagged Securities which have been pledged in their favour.



The Registrar of Securities Services (Registrar) recently published proposed amendments to the Strate Rules for public comment under s71 of the Financial Markets Act, 2012 (FMA). The main purpose of the proposed amendments is to consolidate the Strate Rules dealing with equity securities, bond securities and money market securities (Securities). In order to consolidate and align the Strate Rules, the current s6 (Accounts other than money market securities accounts) and s7 (Money market securities ownership register) of the Strate Rules will be consolidated and renamed "Accounts" and "Settlement" respectively.

A number of editorial changes were made to the Strate Rules to align definitions with the consolidation of the Strate Rules dealing with Securities. However, this alert focuses on the substantive amendments to the Strate Rules which impact on electronic flagging of pledged Securities by Central Securities Depository Participants (CSDPs).

One of the notable amendments to the Strate Rules is the insertion of a new Rule 7.6.2 dealing with a pledge or cession *in securitatem debiti* of the "Securities Account". Currently, under the Strate Rules, a CSDP can only note a security interest in respect of specified Securities in favour of a pledgee or cessionary. However, s39(3) of the FMA states that an interest in respect of uncertificated Securities may be granted in the manner provided for in the Strate Rules, where such an interest extends to all uncertificated Securities standing to the credit of the "Securities Account" at the time the pledge is effected.

In line with s39(3) of the FMA, Strate has now proposed a so-called "wheelbarrow" pledge rule in respect of "Securities Accounts" held in Strate. The "Securities Account" itself may now be pledged or ceded *in securitatem debiti* to the pledgee or cessionary as security for any existing monetary obligations of the pledgor

or ceder. The "Securities Account" (and all of the Securities standing to the credit of such an account at the time that the pledge is effected) may now be electronically flagged in favour of a pledgee or cessionary as an alternative to electronically flagging specific Securities held in a "Securities Account".

In addition, CSDPs are required to send statements to the pledgee or cessionary evidencing the existence of the pledge or cession *in securitatem debiti* over specifically flagged Securities which have been pledged in their favour. However, it is interesting to note that the new Rule 7.6.2 does not place a similar obligation on a CSDP to send such statements to a pledgee or cessionary when the "Securities Account" itself is electronically flagged.

"Segregated Depository Accounts" (SDAs) are now expressly restricted to equity securities only and CSDPs may not hold bond securities or money market securities in SDAs on behalf of clients in SDAs. (An SDA is different from a typical "Securities Account" in that the equity securities held in an SDA on behalf of a client are clearly segregated and distinguishable from the CSDP's equity securities.)

ELECTRONIC FLAGGING UNDER THE CONSOLIDATED STRATE RULES

CONTINUED

CSPDs to send monthly statements to clients in respect of money market securities.



Although CSDPs still need to provide their clients with bi-annual statements in respect of equity and bond securities, Strate has proposed an amendment to Rule 5.8.5 to impose a duty on CSPDs to send monthly statements to clients in respect of money market securities.

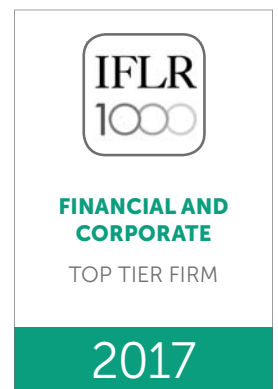
For purposes of s50(3) of the Companies Act, 2008 (which requires that a record be maintained of all uncertificated securities to be administered by a CSDP on behalf of a company) Strate has proposed the insertion of a new paragraph into Rule 6 of the Strate Rules. The new proposed rule provides that a record of ownership in Strate in respect of:

- equity securities must be recorded either in a "Securities Account" held by a CSDP in a "subregister" or in an SDA held by Strate in an "SDA register"; and

- bond securities and money market securities must be recorded in a "Central Securities Account" held by Strate in an "uncertificated securities register".

The proposed amendments to the Strate Rules, once in effect, will align and consolidate the Strate Rules with current market practice. Interested parties were requested to lodge their objections to the proposed amendments by 28 April 2017 and the Registrar's office has indicated that no objections were received. The effective date is currently being decided by Strate and the Registrar's office has indicated that the proposed amendments should come into force before the end of June.

Bridget King and Raaziq Ismail



TACIT FAIS ADVICE

In Gumedé v JDG Trading (Pty) Ltd (Trading as Barnett's) 2009, the FAIS Ombud was faced with a complaint from Ms Gumedé who purchased a small television and a small stove from the respondent.

An offer is merely a proposal made by one person to another indicating his willingness to enter into a contract with him on certain terms.



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'Advice' is defined in FAIS as 'any recommendation, guidance or proposal of a financial nature furnished, by any means or medium, to any client or group of clients'. It also includes a recommendation, guidance or proposal, of a financial nature, on the conclusion of any transaction which is aimed at incurring any liability.

'Advice' may only be given by a qualified and registered financial services provider (FSP), as defined, or a 'representative', as defined, of an FSP.

It is clear that if a person gives advice orally then this will fall within the definition of 'advice'. But what happens if the 'advice' is in writing and one merely points at it and the document is signed by the customer?

In *Gumedé v JDG Trading (Pty) Ltd (trading as Barnett's) 2009*, the FAIS Ombud was faced with a complaint from Ms Gumedé who purchased a small television and a small stove from the respondent. The complainant was given papers to sign by an employee of the respondent. Those papers included, *inter alia*, a schedule to a loan agreement, Goods Insurance Policy and Credit Life Policy. The salesperson produced the documents and showed the complainant where to sign.

The respondent argued that the salesperson did not give advice and as such there was no duty to comply with FAIS.

In *Gumedé*, the Ombud stated that the use of the word "any" in the definition of advice, clearly includes both expressed and implied recommendation and guidance.

It's important to note, as was illustrated in *Gumedé*, that the client had not intended to buy a financial product. The client's primary intention was to buy a television.

A contract is an agreement made with the intention of creating an obligation(s). A contract consists of an invitation to agree to the creation of obligations between the contracting parties and consent thereof (offer and acceptance). An offer is merely a proposal made by one person to another indicating his willingness to enter into a contract with him on certain terms. By showing the client where to sign, the salesperson is making an offer, which may or may not be accepted by the customer. This offer falls within the meaning of proposal, which initiates the application of FAIS

The above scenario and the *Gumedé* case point to a future where more and more, companies need to be aware of the regulatory landscape that they may be falling foul of. The mere pointing out of an insurance policy can be likened to a tacit offer to enter into an insurance agreement which may constitute 'advice', as defined, and therefore the provisions of FAIS apply.

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