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23 November 2015,

Mr Allen Wicomb
The Standing Committee on Finance
Parliament

By e-mail: awicomb@parliament.gov.za

Dear Sirs,

Johannesburg Stock Exchange: Submission to Parliament - Financial Sector Regulation Bill [B35-2015]

1. **Introduction**

1.1 We refer to the Financial Sector Regulation Bill [B34-2015] that was published for comment on 27 October 2015 (the "**FSR Bill**").

1.2 On 6 November 2015, the Standing Committee on Finance (the "**Committee**") published an invitation for written submissions on the FSR Bill. The JSE Limited (the "**JSE**") hereby provides its written submissions to the Committee on the FSR Bill. The JSE also proposes to provide oral submissions to the Committee on 24 November 2015 and/or 25 November 2015.

1.3 Owing to the limited time afforded for making submissions, the JSE does not set out its comprehensive comments on the FSR Bill here. Instead, it has chosen to highlight only the most critical areas of the Bill identified so far. There are also other principle issues of concern that have to be addressed and/or rectified in the Bill and the JSE will supplement and amplify this submission should this become necessary. The JSE's choice to only comment on the critical issues of concern was necessitated by the limited time provided to submit comments to the Committee and does not amount to a waiver of its right to comment on all aspects of legislation that affects the JSE directly and that introduces substantive changes of well-established policies in the regulation of financial market infrastructures.

1.4 This submission shall address the six primary concerns that the JSE, in the limited time available to it, has identified with the FSR Bill:

1.4.1 the inadequate consultation preceding the publication of the Bill;

1.4.2 the provisions governing the licensing of central counterparties;

1.4.3 the provisions dealing with external central counterparties;

1.4.4 the removal of the Directorate of Market Abuse;

1.4.5 the reconsideration provisions of the FSR Bill; and

1.4.6 the powers of the Authority.

2. Inadequate consultation

2.1 Although the current draft of the FSR Bill was preceded by a prior iteration in December 2014, that draft was markedly different to the current draft. For example, a central counterparty was defined in the December 2014 version of the Bill to include both associated and independent clearing houses. The current Bill excludes an associated clearing house from the definition. This creates serious difficulties for the JSE. We deal in more detail with this issue in the next section. The current Bill also introduces for the first time the prospect of an exemption from the licensing requirements for an external central counterparty. This is a highly problematic part of the Bill. As will be explained in more detail in the next section, this has the potential to seriously undermine financial stability and to introduce an inequality in the market that is indefensible. There has been inadequate consultation on these issues.

2.2 The JSE also takes issue with the fact that it has been given less than a month to provide comments on the Bill, which, as set out above, has included radical revisions since the December 2014 iteration.

2.3 In these circumstances, the JSE respectfully submits that the consultation process on the Bill has been inadequate and there has not been a proper assessment of the implications of some of the changes in the Bill. The JSE strongly believes that many aspects of the Bill ought to be rethought in their entirety and further investigations and analysis ought to be conducted of its impact.

3. Licensing of Central Counterparties under the Bill

3.1 <u>Background</u>

3.1.1 JSE Clear (previously known as Safex Clearing Company or SAFCOM) has (since its inception in September 1998) been a clearing house for the South African Futures Exchange ("**Safex**"). In 2001, Safex was purchased by the JSE and has been operating as an "*associated clearing house*" since then. It is an associated clearing house because it acts as a clearing house in accordance with the JSE's Rules and in terms of the clearing agreements concluded between JSE Clear and the clearing members of the JSE.

3.1.2 SAFCOM also historically performed the function of a central counterparty for Safex. A central counterparty is a clearing house that is positioned between counterparties to contracts traded in one or more financial markets. This structure insulates market counterparties from one another's default.[1] This is evidenced as far back as 1988 when rule 8.3.2 of Safex's original rule book stated that:

> "*upon a trade being cleared, by novation the clearing house shall replace the buyer and become the counterparty to the seller and it shall replace the seller and become the counterparty to the buyer.*"

3.1.3 The above wording remains unchanged and is the wording currently used in section 8.30.2 of the latest version of the JSE's Derivatives Rules.

3.1.4 The current version of the Financial Markets Act, 19 of 2012 (the "**FM Act**") defines a "*clearing house*" as:

> "*a person who constitutes, maintains and provides an infrastructure to clear transactions in securities.*"

3.1.5 The current FM Act also defines an "*associated clearing house*" as:

> "*a clearing house that clears transactions in securities on behalf of one or more exchanges in accordance with the rules of the relevant exchange and that does not approve or regulate clearing members.*"

3.1.6 The current FM Act recognises "*independent clearing houses*" that clear transactions in securities on behalf of any person, and authorises and supervises its clearing members in accordance with its clearing house rules.

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[1] Kotze et al "The dilemma of a central counterparty versus a qualified central counterparty in a developing country" *International Conference on Applied Economics (ICOAE) 2014* 1

3.1.7 JSE Clear does not qualify as an independent clearing house under the current Act because it does not authorise or supervise its clearing members in accordance with its own clearing house rules.

3.1.8 The associated clearing house model used by Safex and SAFCOM, and subsequently, JSE Clear and the JSE, was necessitated by the provisions of the Securities Services Act, 36 of 2004 and its predecessor, the Financial Markets Control Act, 55 of 1989 which excluded clearing houses from being classified as self-regulatory organisations. The Securities Services Act defined a "*self-regulatory organisation*" as "*an exchange or a central securities depository*".

3.1.9 This classification had the effect that SAFCOM (as JSE Clear was previously known) was not empowered to promulgate clearing house rules and the contractual arrangements through which SAFCOM managed its affairs were not afforded the protection of section 35A of the Insolvency Act, 24 of 1936 (the "**Insolvency Act**"). Safex and the JSE were therefore obliged to promulgate exchange rules to ensure that all transactions concluded on the exchange and cleared through JSE Clear were subject to the protection afforded by the provisions of section 35A of the Insolvency Act.

3.1.10 The associated clearing house model is therefore recognised and permitted under the provisions of the current FM Act and JSE Clear has the status of a licensed associated clearing house under the current regime.

3.2 Central Counterparties under the FSR Bill

3.2.1 The FSR Bill proposes numerous amendments to the FM Act.

3.2.2 Although it retains the definition of, and references to, an associated clearing house, it introduces a new definition of "*central counterparty*" that excludes associated clearing houses.

3.2.3 Under the Bill, a "*central counterparty*" is defined as:

> "*an independent clearing house that-*
>
> *(a) interposes itself between counterparties to transactions in securities, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the performance of open contracts; and*
>
> *(b) becomes a counterparty to trades with market participants through novation, an open offer system or through a legally binding agreement.*"

3.2.4 An "*independent clearing house*" is defined as:

"a clearing house that clears transactions in securities on behalf of any person in accordance with its clearing house rules, and authorises and supervises its clearing members in accordance with its clearing house rules."

3.2.5 As set out above, JSE Clear does not currently qualify as an independent clearing house because it does not authorise or supervise its clearing members in accordance with its own clearing house rules.

3.2.6 As a result of the manner in which a central counterparty has been defined in the Bill, JSE Clear will also not qualify as a central counterparty because it does not qualify as an independent clearing house.

3.2.7 This has serious ramifications for JSE Clear. If JSE Clear no longer qualifies as a central counterparty under the FM Act, and hence South African law, it will not be able to meet the first requirement for international recognition as a central counterparty.

3.2.8 Moreover, because of JSE Clear's current status as a qualifying central counterparty, all market participants that conclude transactions in securities cleared by JSE Clear qualify for capital relief in accordance with the Basel III principles. If JSE Clear no longer qualifies as a central counterparty because of the particular way in which that term has been defined in the proposed amendments to the FM Act, these market participants' capital relief will fall away and with it, there will be significant disruption to South African markets with the potential result of systemic risk to the South African economy. In addition, if JSE Clear ceases to qualify as a central counterparty as a consequence of the FM Act being amended as is currently envisaged, it may lose its status as a central counterparty recognised and accredited by the Committee on Payment and Settlement Systems ("**CPSS**") of the International Organisation of Securities Commissions Organisation ("**IOSCO")** and many market participants will have no choice but to withdraw from the South African derivatives market. This will invariably result in a massive loss of liquidity in this markets which will again impact negatively on and compromise the integrity of the South African financial markets as a whole.

3.2.9 Chapter V of the FM Act deals with clearing houses. Under the current FM Act, all clearing houses, both independent and associated, have to be licenced under section 49. Under section 50 of the current Act the functions of licenced clearing houses are set out.

3.2.10 The Bill proposes far reaching amendments to this chapter of the Act. It provides not only that clearing houses must be licenced but also that central counterparties must be licensed.[2]

3.2.11 It also defines the functions that a central counterparty may perform. These will be introduced in the new section 50(3A). Under this new subsection, a licensed central counterparty, in addition to other functions set out in the section, must:

(a) interpose itself between counterparties to transactions in securities through the process of novation, legally binding agreement or open offer system;

(b) manage and process the transactions between the execution and fulfilment of legal obligations between counterparties and clients; and

(c) facilitate its post-trade management functions

3.2.12 JSE Clear (through the provisions of the JSE's Derivatives Rules) currently performs all of these functions as an associated clearing house and central counterparty It will therefore face an intractable problem if the Bill is enacted in its current form.

3.2.13 Simply put, JSE Clear, as an associated clearing house, does not qualify as an independent clearing house. However, the Bill seeks to define a central counterparty in terms that recognise only independent clearing houses as central counterparties. Thus, despite the fact that JSE Clear currently performs the functions of a central counterparty, when the Bill takes effect, it will be precluded from performing the functions of a central counterparty because it will not fall within the new statutory definition of a central counterparty.

3.2.14 This problem arises from the particular manner in which the Bill proposes to define a central counterparty. The JSE has previously made representations on earlier versions of the Bill and the Proposed Regulations that preceded it to explain that it does not make sense to define a central counterparty in terms that recognise only independent clearing houses performing the functions of a central counterparty. The definition of a central counterparty should be neutral as between types of clearing houses.

3.2.15 If the definition of a central clearing house is therefore amended to be neutral as between associated clearing houses and independent clearing houses, the problems faced by JSE Clear would be avoided.

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[2] This provision will be contained in section 47(1A) of the FM Act after amendment

3.2.16 Alternatively, if the definition proposed in the Bill is to be retained then it will be necessary for JSE Clear to meet all of the criteria to be licensed as a central counterparty. In order to be licensed as a central counterparty, JSE Clear will need to transform itself into an independent clearing house and then apply for a licence as a central counterparty. To apply for this licence, JSE Clear will need to comply with the following requirements:

3.2.16.1 provide proposed clearing house rules - section 47(3)(c)(v) of the FM Act (as amended by the FSR Bill);

3.2.16.2 implement a margin system that establishes margin levels commensurate with the risks and particular attributes of each product, portfolio and market it serves - section 48(1A)(a) of the FM Act (as amended by the FSR Bill);

3.2.16.3 collect and manage collateral held for the due performance of the obligations of clearing members or clients of clearing members - section 48(1A)(b) of the FM Act (as amended by the FSR Bill);

3.2.16.4 establish and maintain a default fund to mitigate the risk should there be a default by a clearing member and to ensure, where possible, that the obligations of that clearing member continues to be fulfilled - section 48(1A)(c) of the FM Act (as amended by the FSR Bill);

3.2.16.5 supply initial capital as prescribed, including the appropriate buffer - section 48(1A)(d) of the FM Act (as amended by the FSR Bill);

3.2.16.6 have a clearly defined waterfall where the obligations of the defaulting clearing member, other clearing members and the central counterparty are legally and clearly managed - section 48(1A)(e) of the FM Act (as amended by the FSR Bill);

3.2.16.7 provide for portability in the case of default of a clearing members - section 48(1A)(f) of the FM Act (as amended by the FSR Bill); and

3.2.16.8 provide the necessary infrastructure, resources and governance to facilitate its post trade management function, and in the event of one or more of the clearing members:

3.2.16.8.1 ensure sufficient risk policies, procedures and processes; and

3.2.16.8.2 have sound internal controls for robust transaction processing and management - section 48(1A)(g) of the FM Act (as amended by the FSR Bill).

3.2.17 Complying with these requirements will require various structures to be put in place, documentation to be drafted and/or amended, and other transitional arrangements (including capital arrangements) to be made.

3.2.18 JSE Clear cannot do so overnight and therefore requires a reasonable period of time within which to put these structures and arrangements in place.

3.2.19 It appears that the Bill contemplates the need for a delayed implementation of the licencing for central counterparties. It proposes to introduce a new subsection in section 110. The new subsection (6) reads as follows: "*With effect from a date prescribed by the Minister, a licensed clearing house performing the functions of a central counterparty must be licensed as a central counterparty under section 49 and comply with the requirements set out in this Act*".

3.2.20 The provision appears to speak to the situation in which JSE Clear will find itself when the Bill is enacted. It will be performing the functions of a central counterparty but will not be able to be licensed as such until it can comply with the new requirements. Section 110(6) therefore appears to contemplate a delayed implementation of this licensing requirement to permit the Minister to designate a future date by which parties performing the functions of a central counterparty must be licensed to do so.

3.2.21 This delayed implementation of to the licensing obligation is not, however, reflected in section 47 of the FM Act itself where the obligation to be licensed is contained in the Act. It would therefore be preferable for a cross reference to section 110(6) to be inserted into section 47(1A). The current wording of that new section in the Bill reads as follows:

> "*Subject to the regulations prescribed by the Minister, a central counterparty must be licensed under section 49*"

3.2.22 It is unclear what regulations the proviso is referring to. It would be preferable for this section to be worded as follows: "*subject to section 110(6), a licensed clearing house performing the functions of a central counterparty must be licensed as a central counterparty under section 49*".

3.2.23 In order to make it clear that a licensed clearing house may continue lawfully to perform the functions of a central counterparty despite not being licensed as such, the JSE respectfully submits that it would be prudent to add a further subsection to section 110 to the effect that

"notwithstanding any other provision of this Act, until the date prescribed by the Minister under subsection (6), a licensed clearing house may continue to perform the functions of a central counterparty despite not being licensed to do so."

3.3 Summary of the JSE's submissions regarding the licensing regime proposed for central counterparties under the Bill

3.3.1 For the sake of convenience, the JSE provides below a brief summary of its submissions on the above point.

3.3.2 For historical reasons, JSE Clear functions as an associated clearing house. In order to permit it to continue to perform its important function as a central counterparty under the FM Act, either:

3.3.2.1 The definition of "*central counterparty*" should be amended to be neutral as between types of clearing houses; or

3.3.2.2 Sections 57(1A) and 110 should be amended to make it clear that until a date prescribed by the Minister, an existing licensed clearing house may lawfully perform the functions of a central counterparty without being licensed as such.

4. External central counterparties

4.1 The Bill also introduces a new definition of an "*external central counterparty*". This is:

"a foreign person who is authorised by a supervisory authority to perform a function or functions similar to one or more of the functions of a central counterparty as set out in this Act and who is subject to the laws of a country other than the Republic, which laws (a) establish a regulatory framework equivalent to that established by this Act; and (b) are supervised by a supervisory authority".

4.2 A supervisory authority is defined in the FM Act as "a *body designated in national legislation to supervise, regulate or enforce legislation or a similar body designated in the laws of a country other than the Republic to supervise, regulate or enforce legislation of that country*".

4.3 Chapter V of the FM Act will be amended by the Bill to introduce the concept of, and requirements for, the licensing of external counterparties.

4.4 The proposed amendments will make it a requirement for external counterparties to be licensed under section 49A of the FM Act, unless they are exempted from having to be licensed under section 49B.

4.5 Under section 49B, external counterparties may apply to the Authority to be exempted from the requirement to be licensed under section 49A.

4.6 The Authority is then empowered (provided it has the concurrence of the Prudential Authority and the South African Reserve Bank) to grant such an exemption if four requirements are met:

4.6.1 The applicant is recognised under section 6A;

4.6.2 The applicant is subject to an appropriate regulatory and oversight regime in the foreign country by the relevant supervisory authorities;

4.6.3 The applicants agrees to co-operate and share certain information; and

4.6.4 The granting of the exemption will not compromise the objects of the Act.

4.7 The objects of the FM Act are set out in section 2. They include ensuring that the South African financial markets are fair, efficient and transparent (section 2(a)) and reducing systemic risk (section 2(d)).

4.8 The JSE respectfully submits that permitting an exemption from the requirements of licensing is in conflict with these objectives.

4.9 An exemption for external central counterparties introduces unfairness into the South African financial markets because it permits certain providers to be exempt from licensing requirements while they provide the same services as their local counterparts who are required to be licensed.

4.10 It also has the potential to undermine financial stability and introduce systemic risk. It has been recognised in South Africa and abroad that in order to ensure financial stability system-wide risk needs to be managed through a macro-prudential regulatory approach. The regulatory approach needs to be of universal application in order to reduce the risk of regulatory arbitrage.

4.11 If external central counterparties are exempted from the oversight of South African authorities, their regulation is effectively outsourced to foreign regulators. This denudes any oversight and or regulatory role that the South African authorities may wish to fulfil in respect of entities.

4.12 In the event of an economic crisis, such as the one experienced in 2008, the consequences arising from this deficiency could be severe.

4.13 South Africa was largely insulated from the recent financial crises as a result of the robust risk management policies of JSE Clear and the fact that, in terms of the JSE's rules, collateral and assets are

segregated to client level. This in turn precludes the so called "re-hypothecation" of collateral and the co-mingling of assets of market participants. For example, client A has concluded a client agreement with authorised user (trading member) M. A posts R 100 000 margin to JSE Clear as collateral for the due performance of its obligations on the derivatives market. Member M is insolvent as a result of large trading losses but all its clients' margin and assets do not fall within its insolvent estate as a result of the segregation of client assets provided for in the JSE Rules. All the clients of M will be ported to another trading member, M's positions will be closed out but its clients' positions, assets and collateral will be unaffected. In addition hereto, all the collateral held is held in South Africa and JSE Clear will have immediate access to margin posted to ensure due performance of a defaulter's obligations. This will however not be the case in many international jurisdictions where "re-hypothecation" of collateral is permissible and where assets and collateral are not segregated down to client level. In these jurisdictions it is permissible that M may use A's R 100 000 as collateral for its own obligations (the R 100 000 will be "re-hypothecated"). M's default will also result in A's default and clients will not be protected and insulated from the default of trading member M. This will expose the South African financial markets to unknown and unlimited risks from jurisdictions over which the South African regulatory authorities have no control. It is therefore of critical importance that the South African authorities have direct and effective regulatory oversight over all central counterparties that conduct business in South Africa.

4.14 The JSE recognises that the cross border nature of financial markets requires an appropriate supervisory and cooperative regulatory framework should external central counterparties wish to perform functions within South Africa. However, removing the requirement of licensing is in the JSE's considered opinion not the appropriate way to achieve this co-operation. If external central counterparties are to fulfil the same duties and functions as local ones, fairness and the stability of the South African financial system requires that the South African authorities themselves regulate the business of these external entities and not abdicate that responsibility to foreign authorities. Regulatory oversight of all market infrastructures operating in South Africa is key to ensuring the stability of the South African financial system. .

4.15 It is a condition of the licences of local central counterparties that they fulfil certain duties prescribed under the FM Act (see sections 59(2) and (3)). Under the current FM Act, if a local central counterparty fails to fulfil its duties and responsibilities, the Registrar may directly assume responsibility for one or more of these functions and duties (see section 50(4) of the FM Act). Under the proposed amendment to the FM Act, there will be no equivalent oversight role for the Registrar in relation to external central

counterparties nor will the Registrar have the power to directly assume responsibility for the fulfilment of these important duties and functions.

4.16 It may well be that an external central counterparty is subject to a similar regulatory regime in an international jurisdiction but if it is exempted under section 49B, the South African authorities will have no control over the external central counterparty's risk management methodologies. The authorities will not be able to prescribe the type of collateral and manner in which collateral is held nor will they be able to have immediate access to margin and other collateral held in a foreign jurisdiction in which the external central counterparty is domiciled. It is also unavoidable that assets and collateral that were earmarked to fulfil obligations in the South African markets will be tied up or used to fulfil other obligations as a result of an international crisis.

4.17 Because such exemptions are inconsistent with two of the primary objects of the FM Act, it would, in the JSE's opinion, never be lawful for the Authority to grant an exemption under section 49B(3)(d). On its own terms, that section requires an exemption to be granted only if it would not compromise the objects of the Act. However, permitting an exemption at all is inconsistent with the objects of fairness and ensuring financial stability.

4.18 The introduction of an exemption regime that is inconsistent with the objects of the FM Act and that could accordingly never permit a lawful exemption to be issued, would be irrational.

4.19 If the exemption provisions of section 49B are introduced into the FM Act, they would be liable to challenge on the basis of irrationality. The JSE therefore submits that they should be deleted.

4.20 Over and above the exemption provisions for external central counterparties, there is also an inconsistency introduced into the FM Act between the treatment of local and external central counterparties.

4.21 In terms of the provisions of the FM Act, financial market infrastructures ("**FMIs**") fulfil licensed duties and functions (Section 10 – exchanges, section 30 CSDs and section 50 clearing houses). FMIs authorise users, clearing members and participants to provide securities services, as defined, in terms of the rules of the FMI and an integral part of the FMI's licensed duties and functions is the supervision and regulation of the securities services provided by these authorised participants.

4.22 In terms of the general regulatory framework envisaged under the FM Act, it is not permissible for FMIs to provide securities services themselves, inter alia as a result of the insoluble conflicts of interests that it will cause if they do so. The proposed new section 49A(1) however states that an external central

counterparty *"may provide securities services"*. This is inconsistent with the provisions applicable to local FMIs.

5. Directorate of Market Abuse

5.1 One of the significant (and highly problematic) proposed amendments to the FM Act is the discontinuation (and dissolution) of the Directorate of Market Abuse (**"DMA"**) through the repeal of section 85 of that Act. This raises concerns for the JSE in our role as a market regulator, market operator and a stakeholder in the fight against market abuse. We previously raised these concerns in our comments on the draft FSR Bill published in December 2014 but they have unfortunately not been taken on board.

5.2 The rationale for the repeal of section 85 appears to be reflected in National Treasury's response to the JSE's previous comments as follows:

> *"In the interests of harmonisation and rationalization of administrative processes and procedures across the financial sector, the DMA has been replaced by the FSCA directly. The FSR Bill does allow however for the FSCA to create administrative action committees. Such administrative action committee/s will allow for a more flexible approach that provides the same set of powers for all administrative actions by the FSCA, and not just those that relate to the FMA. A specialist DMA type panel can therefore be established in the new regime. It does not need to be specifically named as such."*

5.3 From the above comment it appears that National Treasury is supportive of the establishment of the equivalent of the DMA by the Financial Sector Conduct Authority (**"FSCA"**) but that the establishment of such a committee would be in terms of the administrative action committee provisions in the FSR Bill.

5.4 It is common cause that South Africa is highly regarded for the regulation of its securities markets. Market abuse is probably the most visible form of market misconduct in terms of the impact that it has on investors' perceptions of the integrity of a market. Investor confidence is built on a combination of factors but local and international investors' perceptions of the extent of market abuse in a market and the effectiveness of anti-market abuse regulation and enforcement is one of the key pillars in building that confidence. The effectiveness of the regulatory structures in South Africa in combatting market abuse is one of the big success stories in financial sector regulation in this country. The DMA has contributed significantly to that success as it brings together individuals with valuable skills and knowledge from a variety of relevant disciplines to provide input on important decisions during the enforcement process.

5.5 In exercising certain powers of the FSB under the FM Act, the DMA is not an administrative body and it does not make enforcement decisions. It considers matters that have been brought to the attention of the FSB's Department of Market Abuse and the results of the work undertaken by that department in relation to those matters, and through the collective knowledge and experience of its members, it determines whether a matter merits further investigation, provides guidance on aspects of the investigation and ultimately determines whether a matter should be referred for enforcement action, either administrative or criminal.

5.6 Under the FSR Bill, the FSCA will have extensive enforcement powers, including the power to investigate market abuse. The necessary powers to conduct investigations and prosecute market abuse will therefore continue to exist. However, the DMA currently plays an important and valuable role that supports the investigative process and essentially sits between the investigation and the enforcement action and it is that role that will be lost if section 85 of the FM Act is repealed.

5.7 A market conduct regulator typically has a good understanding of the market abuse provisions that it is enforcing and possesses effective investigative skills. However, it would not necessarily possess the insight into the trading strategies and business activities of the entities from which market abuse may originate. Furthermore, whilst a market conduct regulator will naturally possess legal skills it can often benefit from the insights of legal professionals who are steeped in some of the legal complexities associated with the prosecution of offences such as market abuse and who can provide useful input into the scope and focus of investigations and the decisions on whether or not to initiate enforcement action. The DMA has brought together these skills and insights in a very effective manner over the past 15 years. This combination of skills has enabled it to make a significant contribution to the effectiveness of the enforcement structures in South Africa and the fight against market abuse.

5.8 This unique role will not be able to be fulfilled through the administrative action committee provisions in the FSR Bill.

5.9 National Treasury's comment above appears to propose that a specialist DMA-type committee can be established in terms of the broad administrative action provisions of the FSR Bill but that the legislation does not have to specifically name (implying "create") such a committee. However, it is clear from the provisions of section 87 of the Bill dealing with the functions and composition of an administrative action committee that a committee established in terms of that section is intended to be an administrative body either recommending specific administrative action to be taken by the FSCA or, through delegated powers, taking administrative enforcement action on behalf of the FSCA. These administrative action committees are therefore essentially enforcement committees. In order to either

recommend what administrative action should be taken or to take such action itself, an administrative action committee would need to consider both the administrative and legal issues to make a finding. It is for this reason that the composition of an administrative action committee must, in terms of section 87(3) of the Bill, include a retired judge or an advocate or an attorney with at least ten years' experience. The DMA has never fulfilled this function and therefore the provisions of section 87 of the Bill will not enable the establishment of a specialist committee equivalent to the DMA.

5.10 Market abuse is a unique issue that requires and has benefited from a unique approach. It is not a subject that pertains to a particular regulated industry as is the case with other financial services legislation. It is an issue of conduct that spans the activities of issuers of securities and investors from various industries as well as investors who are not regulated by any other legislation in relation to their investment activities (such as retail investors). Unlike most other financial sector legislation it is not about the services or the protection provided by a regulated entity to its customers or investors; it is about the impact that the actions of participants in a market can have on each other and on the confidence that market participants (both local and foreign) have in the integrity of the South African financial markets. It is for this reason that an approach that simply seeks to "*harmonise and rationalise processes*" across the entire financial sector is not suited to the unique challenges that we face in combatting market abuse.

5.11 The skills, experience and knowledge of individuals who collectively have insight into, and an understanding of, the activities and objectives of the numerous issuers and investors participating in the financial markets and who understand the legal complexities of applying market abuse legislation has proven to be extremely valuable for the past 15 years in promoting the objectives of the FM Act and supporting the good work of the FSB. Harnessing the valuable contribution that those individuals can make during the enforcement process requires the law to specifically recognise the function that a committee made up of those individuals should perform. This cannot be achieved through legislation that makes broad provision for administrative action structures that can be applied uniformly to all matters that fall within the regulatory jurisdiction of the FSCA.

5.12 If the intention behind the creation of the administrative action committees is to retain the existing structures (or the equivalent thereof) that have proven to be successful in combatting market abuse but to provide the FSCA with greater flexibility in achieving the objectives of those structures then this can be achieved through appropriate amendments to the FM Act that provide for the establishment and operation of a market abuse committee with the appropriate functions but which provide greater flexibility to the FSCA in relation to matters such as the composition and activities of the committee. These operational matters can be left to the FSCA to manage. The JSE would support such an approach.

5.13 Harmonising and rationalising existing processes by discontinuing the DMA should not come at the expense of weaking the structures that have proven to be effective in the fight against market abuse. The JSE therefore submits that the FM Act should continue to make provision for the establishment of a specialist committee such as the DMA but that the FSCA be granted the powers to determine the composition and procedures of the committee.

6. The reconsideration provisions of the FSR Bill

6.1 Section 94 of the FSR Bill empowers a financial sector regulator to reconsider a decision it has made either on its own initiative or on written application by an aggrieved person. The section places no limit on the number of times that a financial sector regulator can reconsider a decision it has made.

6.2 Under section 1 of the FSR Bill, the FSCA is a financial sector regulator and thus section 94 of the Bill applies to its decisions.

6.3 Under the FSR Bill's proposed amendments to the FM Act, the FSCA is the Authority that makes many of the decisions under the FM Act, including, for example, the decision whether to grant a licence application to be a central counterparty.

6.4 The decisions of the FSCA to grant or refuse an application for a licence under the FM Act would constitute administrative action under the Promotion of Administrative Justice Act 3 of 2000 ("**PAJA**").[3] The decisions would accordingly be subject to review under PAJA.

6.5 However, section 7(2)(a) of PAJA provides that no court or tribunal shall review an administrative action unless an internal remedy provided for in any other law has first been exhausted.

6.6 Section 94 of the FSR Bill provides an internal remedy for persons aggrieved by decisions of the FSCA. However, because it is unclear how many times the FSCA can be approached for a reconsideration of its decisions taken under the FM Act, it is unclear when that internal remedy of reconsideration will be exhausted for the purposes of section 7(2)(a) of PAJA.

6.7 The JSE therefore respectfully submits that this section requires amendment to make it clear when the process of reconsideration ceases and aggrieved parties may approach the courts for relief.

7. Powers of the FSCA

[3] Grey's Marine Hout Bay (Pty) Ltd and Others v Minister of Public Works and Others 2005 (6) SA 313 (SCA) paras 21 and 22

7.1 If the FSR Bill is enacted, it will amend section 6(3)(k) of the FM Act to provide that the FSCA may issue guidance notes and binding interpretations on the application and interpretation of the Act.

7.2 The FSCA is an administrative body; it is not a court of law. And yet, section 6(3)(k) purports to give any interpretation of the FM Act that it issues, the status of a court order because the section provides that its determinations will be binding. This is inconsistent with section 165(2) of the Constitution which entrenches the independence of the courts. Section 165(2) provides that the courts are subject only to the Constitution and the law. However, the proposed new section of the FM Act purports to give the FSCA the power to issue binding determinations on the proper interpretation of the FM Act and thereby make the courts subject to the determinations of this administrative body. This is incompatible with the independence of the courts.

7.3 The JSE respectfully submits that, if enacted, this section would be unconstitutional.

8. For all the reasons set out above, the JSE believes that the current draft of the FSR Bill suffers from a number of serious deficiencies and shortcomings. The JSE trusts that the Committee will consider the above submissions (which are aimed at curing the problems associated with the FSR Bill) favourably.

Yours faithfully

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