



Financial Sector
Conduct Authority

**NOTICE REGARDING THE PUBLICATION OF DRAFT CONDUCT STANDARD [-] OF 2020
(FM)**

CONDUCT STANDARD FOR EXCHANGES

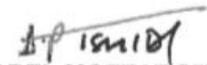
FINANCIAL MARKETS ACT, 2012

FINANCIAL SECTOR REGULATION ACT, 2017

The Financial Sector Conduct Authority (FSCA) hereby invites, in accordance with section 98(1)(a)(iv) of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (FSR Act), submissions on draft Conduct Standard [-] of 2020 (FMA) - Conduct Standard for Exchanges, to be made in terms of section 106(1)(a) read with section 106(2)(a) of the FSR Act and section 17(2A) of the Financial Markets Act, 2012 (Act No. 19 of 2012), as per the Schedule below.

The draft conduct standard, together with a statement supporting the draft conduct standard, is available on the FSCA's website.

Submissions on the draft conduct standard must be submitted in writing, using the submission template available on the FSCA's website, on or before **15** July 2020 to the FSCA at FSCA.RFDStandards@fsc.co.za.


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For THE FINANCIAL SECTOR CONDUCT AUTHORITY

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SCHEDULE

DRAFT CONDUCT STANDARD [-] OF 2020 (FM)

CONDUCT STANDARD FOR EXCHANGES

1. Definitions and interpretation

- (1) In this Schedule, “**the Act**” means the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) and “the Financial Markets Act” means the Financial Markets Act, 2012 (Act No. 19 of 2012) and any word or expression to which a meaning has been assigned in the Act or the Financial Markets Act bears the meaning so assigned to it, and unless the context otherwise indicates-

“**Authority**” means the Financial Sector Conduct Authority as defined in section 1 of the Financial Markets Act;

“**best execution**” means the duty of an authorised user to obtain the best possible result for a client when trading in securities on behalf of that client;

“**cautionary announcement**” means an announcement that an issuer must publish immediately after an issuer becomes aware of any price sensitive information of which the necessary degree of confidentiality cannot be maintained or of which the issuer suspects that confidentiality has or may have been breached;

“**cooperative arrangement**” means an arrangement between licensed exchanges that describes the intentions of the exchanges to cooperate with each other in the performance of their functions under the Financial Markets Act and to address the matters as contained in this Conduct Standard;

“**default**” means a situation when an authorised user is unable to meet its commitments to another authorised user, the exchange, the clearing house or a securities settlement system, arising out of a transaction or a securities settlement system instruction and, for purposes of purposes of paragraph 4(1)(e), an authorised user is also regarded to be in default if -

- (a) an insolvency proceeding has commenced against the authorised user; or
- (b) the exchange, in its sole discretion, declares that an act of default has occurred;

“**dual authorised user**” means an authorised user that has been admitted as an authorised user by more than one exchange in terms of the rules of the respective exchanges;

“**dual listed securities**” means securities included in the list of securities of more than one exchange;

“**failed trade**” means a transaction in securities which either the client, authorised user, the exchange or the clearing house is unable to ensure that such transaction will settle on the settlement date or any revised settlement date;

“**primary exchange**” means the exchange on which an issuer has elected to be primary listed or is deemed by an exchange to be primary listed, based on the value and volume traded in the issuer’s security on that exchange;

“primary listing” means in relation to a security listed on more than one exchange, a listing by virtue of which the issuer is, in respect of that security, subject to the full requirements applicable to listing on that exchange;

“price sensitive information” means unpublished information that is specific or precise, which if it were made public, would have a material effect on the price of the issuer’s securities;

“significant event” means –

- (a) any material systems failure, malfunction, delay or other disruptive system incidents;
- (b) any breach of data security, integrity or confidentiality; and
- (c) developments in the market infrastructure that might reasonably be expected to affect other regulated entities, clients and investors;

“transparency” means the degree of disclosure which enables market participants to obtain information about the trading process, for example price, order size, trading volume, risk and trader identity

“volatility controls” means pre- or post-trade controls that prevent certain orders from being matched.

2. Cooperative arrangements

- (1) Exchanges that have dual authorised users and dual listed securities must enter into a cooperative arrangement with one another on the subject matter contained in this Standard.
- (2) A cooperative arrangement referred to in subparagraph (1) must –
 - (a) provide for alignment of market operations requirements and requirements relating to instances of extreme price movements for harmonised automated pre-trade and post-trade volatility controls;
 - (b) provide for a process to ensure exchange rules and listing requirements in respect of dual listed securities are aligned;
 - (c) make provision for dispute resolution mechanisms to address disputes emanating from the cooperative arrangement;
 - (d) provide for the manner in which price sensitive information will be disseminated simultaneously by all exchanges;
 - (e) be reviewed annually; and
 - (f) provide for the termination of the arrangement if the exchanges no longer have dual authorised users or dual listed securities.
- (3) An exchange as contemplated in subparagraph (1) must provide the Authority with a written progress report on its compliance with, or proposed actions to be implemented in order to comply with, subparagraph (1), within 90 days after the commencement date of this Conduct Standard.
- (4) An exchange must provide the Authority with a copy of each cooperative arrangement (as referred to in subparagraph (1)) –
 - (a) entered into within 14 days of the exchanges concluding such cooperative arrangement;
 - (b) when any material change is made to such agreement.
- (5) An exchange may not admit an authorised user that has also been admitted as an authorised user of another exchange unless it has entered into a cooperative arrangement with that exchange.
- (6) An exchange must notify the Authority –

- (a) before a cooperative agreement is terminated and the reasons for such proposed termination; or
- (b) without delay should it fail to conclude a cooperative arrangement or reach agreement on any matter contained in this Conduct Standard relating to cooperative arrangements.

3. Additional requirements with which exchange rules must comply

- (1) The exchange rules must, in addition to the requirements listed in section 17(2) of the Financial Markets Act, provide –
 - (a) for authorised users to establish and maintain an adequate, effective and on-going process of risk management, which -
 - (i) are consistent with the nature, complexity and risk inherent in the authorised user's on-balance sheet and off-balance sheet activities;
 - (ii) respond to changes in the authorised user's environment and conditions; and
 - (iii) must include the maintenance of effective capital management by an authorised user;
 - (b) for capital adequacy requirements of authorised users that must consist of at least the following –
 - (i) working capital which is the higher of an amount determined in accordance with the exchange's rules or directives as being adequate to meet an authorised user's fixed expenditure for a period of 13 weeks or R500 000; and
 - (ii) adjusted liquid capital, which complies with the minimum requirements of the exchange calculated in accordance with the exchange's rules or directives sufficient to meet its base amount and its risk requirement;
 - (c) for alignment of settlement cycles in respect of dual listed securities;
 - (d) for procedures relating to the notification of other exchanges when transactions effected between dual authorised users are declared failed trades;
 - (e) for arrangements for the exchange to manage an authorised user's default;
 - (f) in respect of dual authorised users trading in dual listed securities, -
 - (i) that the dual authorised user discloses and agrees with its clients how it intends to achieve best execution, taking into account-
 - (aa) the best bid or offer;
 - (bb) the total trading costs;
 - (cc) certainty or likelihood of execution;
 - (dd) the speed of execution;
 - (ee) different exchanges available;
 - (ff) the liquidity of the market at the time of placing the order and execution;
 - (gg) conflicts of interest;
 - (hh) the size and nature of the order;
 - (ii) assurance of settlement; and
 - (jj) the objectives of the client and the priorities the client has placed upon the authorised user in terms of the mandate;
 - (ii) that authorised users must have policies and procedures on how they achieve best execution for clients, taking into account the factors listed in subitem (i);
 - (g) for a clear definition of "erroneous trades" and have aligned requirements and criteria for cancelling such trades, which may include the following:
 - (i) The trade has been matched as a result of an error;
 - (ii) the price is a certain percentage or more away from the reference price;
 - (iii) the quantity of shares traded exceeds a certain percentage of the equity security in issue;
 - (iv) the minimum difference between the aggregate value of the trade and the value that would have resulted had such trade been executed at the reference price is a certain amount or more;
 - (v) if the trade materially impacts the integrity or transparency of the market;
 - (vi) if the trade materially impacts the correctness of the statistics released by the exchange; or

- (vii) if the quantity of securities traded or the price thereof is unreasonable;
- (h) in respect of dual listed securities, for responses to significant events and the procedures to be followed as well as the circumstances under which a trade disruption may occur (trade disruption rules);
- (i) in respect of dual authorised users and dual listed securities, for automated pre-trade or post-trade volatility controls, such as circuit breakers and regulatory halts in respect of individual securities or for the whole market, to ensure the quality of price formation;
- (j) for minimum requirements for comparable or the same type of off-order book trades or off-market trades, which must include-
 - (i) qualifying securities;
 - (ii) reporting requirements and responsibilities;
 - (iii) minimum order sizes and number of times of the exchange market size; and
 - (iv) whether the trade requires public notification.

4. Requirements for exchanges

Time synchronisation to a primary standard

- (1) An exchange must synchronise its clock to the primary standard of measurement for time in the Republic to ensure the precision and accuracy required for time sensitive trading strategies.
- (2) The timescale must be disseminated via an agreed method that would provide for-
 - (a) a correction for network delays;
 - (b) server authentication;
 - (c) server health information;
 - (d) server accuracy information; and
 - (e) leap second notification.
- (3) An exchange must regularly monitor the clock it uses for recording the time and date of trades and implement compliance monitoring and reporting systems to ensure that it remains synchronised to the agreed timescale, within an allowable tolerance level.

Trading disruptions and significant events

- (4) An exchange must inform other exchanges with which it has entered into a cooperative agreement in respect of dual authorised users or dual listed securities without delay of a trading disruption or significant event and must communicate such event to the Authority within 14 days.
- (5) For purposes of subparagraph (4), a trading disruption includes, but is not limited to:
 - (a) the closure of the whole market due to a technical outage of the exchange's trading system;
 - (b) a trading halt or the suspension of a specific security due to, among others, the following reasons:
 - (i) trading activity in a security is being undertaken by persons in possession of unpublished price-sensitive information that relates to that security;
 - (ii) trading activity is being influenced by a manipulative or deceptive trading practice;
 - (iii) trading activity may otherwise give rise to an artificial price for that security; or
 - (iv) the removal of the security from the list of securities.
- (6) A cooperative arrangement referred to in paragraph 2(1) must provide for the following minimum requirements for the release of price sensitive information:
 - (a) the distribution channel for the dissemination of price sensitive information and cautionary announcements, which must be approved by the Authority;

- (b) the format and layout of the information and announcements;
- (c) where the distribution channel should be housed;
- (d) how costs associated with the distribution channel will be apportioned; and
- (e) who will be responsible for the validity of the information that will be disseminated into the market.

Reference price

- (7) In respect of the same securities listed on more than one exchange, the primary exchange's reference prices must prevail, and the primary exchange remains the custodian of the reference price, unless the applicable exchanges decide otherwise, in order to prevent regulatory arbitrage and to ensure consistency and transparency in the market for the determination of:
 - (a) the weighted average traded price used by an issuer for cash resolutions (general and specific/related party);
 - (b) company and portfolio valuations for corporate actions; and
 - (c) market capitalisation for transaction categorisation purposes.

Corporate actions

- (8) In respect of the same securities listed on more than one exchange, the primary exchange is responsible for the corporate actions process and the timetable, in close consultation with the secondary exchange, especially where the corporate action has an impact on the secondary exchange from a clearing and settlement perspective, to ensure that financial customers will, in the interest of fair treatment of financial customers, receive the same entitlements and on the same timetable.
- (9) Pursuant to subparagraph (8), the listing requirements of the primary exchange and its clearing and settlement process must determine and dictate the corporate actions process.

Suspensions and removal of securities from the list of securities

- (10) In respect of the same securities listed on more than one exchange, the listing requirements of the applicable exchanges must be aligned to coordinate and synchronise their processes to ensure consistency in respect of the suspension or the removal of securities from the list of securities, whether it is at the instance of the issuer or the exchange concerned.
- (11) In respect of the same securities listed on more than one exchange, a suspension of a primary listing at the request of an issuer must be made by the primary exchange.
- (12) If an exchange envisages to place securities into a trade suspension or to lift a trade suspension, or to remove securities from the list of securities, all other exchanges where those securities are listed, must be informed timeously to enable the exchanges to take the same action simultaneously.

Default of dual authorised users

- (13) In the event of a default of dual authorised users, exchanges must-
 - (a) coordinate their efforts, consult and share information with
 - (i) other exchanges of whom the authorised user is also a member;
 - (ii) the central securities depository; and
 - (iii) the participant of the defaulting member;
 - (iv) to determine whether cross-exchange netting is possible, and if not, that the rules of each exchange apply;

- (b) minimise the contagion risk that the cross-exchange netting or set-off of transactions across exchanges would afford; and
- (c) provide a notice to the effect that the authorised user has been declared to be in default to all other exchanges of which the authorised user is a member.

5. Short title, commencement date and transitional arrangements

- (1) This Conduct Standard is called the Conduct Standard for Exchanges, 2020 and comes into operation on the date of publication.
- (2) An exchange which has dual authorised users or dual listed securities with another exchange must, within six months from the commencement date of this Conduct Standard amend or replace its rules in accordance with the Act to comply with the requirements of this Conduct Standard.