

DIRECTIVE 2014/17/EAC OF THE COUNCIL OF MINISTERS

of

(Date of Approval by Council of Ministers)

DIRECTIVE OF THE EAC ON INVESTOR COMPENSATION FUNDS

PREAMBLE:

The Council of Ministers of the East African Community

Having regard to the Treaty for the establishment of the East African Community and in particular Articles 85 (d), 14 and 16;

WHEREAS Article 31 of the Protocol on the Establishment of the EAC Common Market provides that for proper functioning of the Common Market, the Partner States undertake to co-ordinate and harmonise their financial sector policies and Regulatory frameworks to ensure the efficiency and stability of their financial systems as well as the smooth operations of the payment system;

WHEREAS Article 47 of the Protocol on the Establishment of the EAC Common Market provides that the Partner States shall undertake to approximate their national laws and to harmonise their policies and systems for purposes of implementing this Protocol and that the Council shall issue directives for the purposes of implementing this Article.

HAS ISSUED THIS DIRECTIVE

ARTICLE 1

INTERPRETATION

For the purposes of this Directive:

“Collective Investment Schemes” (in this Directive shall be referred to as “CIS”) means schemes as defined in Article 2 of the EAC Directive on Collective Investment Schemes;

“Community” means the East African Community established by Article 2 of the Treaty;

“Competent Authority” means the national regulatory agency that is the primary supervising entity of securities markets in the Partner State;

“investor” means a person who has invested in securities in the EAC securities market through any of the market intermediaries in the EAC Community;

“investor compensation fund” means a Fund established for the purposes of granting compensation to investors who suffer pecuniary losses resulting from the failure, of a Market Intermediary to meet their contractual obligations;

“market intermediary” means a broker, dealer, fund manager, investment bank or any other licensed entity by any competent authority in the EAC Community to provide services in the securities market;

“Partner State” means the Republic of Uganda, the Republic of Kenya, the United Republic of Tanzania, the Republic of Rwanda and the Republic of Burundi and any other country granted membership to the Community under Article 3 of the Treaty; and

“Treaty” means the Treaty establishing the East African Community and any annexes and protocols thereto;

ARTICLE 2

OBJECTIVES

The objective of this Directive is to harmonize the standards pertaining to Investor Compensation Funds in the securities markets of Partner States with a view:

- (a) to protect investors by setting the level of compensation payable to investors under the Directive up to a maximum of US\$1,000;
- (b) to reduce systemic risks by setting out in more detail how investor compensation funds should be administered and funded to ensure their sound operations;
- (c) to provide cooperation between investor compensation funds;
- (d) to reduce delays in the pay out of claims to investors;
- (e) to provide for criteria for compensation for investors;
- (f) to provide for investors to receive more detailed information from market intermediaries about what is covered and not covered under compensation fund.

ARTICLE 3 PRINCIPLES

In implementing this Directive, Partner States shall abide by the following principles:

- (a) ensure confidence in capital markets by promoting high standards of transparency and prompt payment of compensation;
- (b) provide investors with a reasonable level of disclosure and protection tailored to their circumstances;
- (c) ensure that Competent Authorities enforce the rules consistently, in relation to the establishment of mandatory compensation funds; and
- (d) ensure coherence across Partner States' legislation on investor compensation funds.

ARTICLE 4 SCOPE

This Directive shall apply to all investor compensation funds established in respect of the Securities Markets within the Community.

ARTICLE 5 ESTABLISHMENT OF INVESTOR COMPENSATION FUNDS

1. Each Competent Authority shall ensure that within its territory one or more investor-compensation funds are introduced and officially recognised.
2. A fund shall provide coverage for investors in relation to securities business in accordance with Article 4 where any of the following conditions apply:
 - (a) the Competent Authorities have determined that a market intermediary appears, for the time being, for reasons directly related to the financial circumstances of the market intermediary or the financial circumstances of any third party with whom financial instruments have been deposited by the market intermediary, to be unable to meet its obligations arising out of investors' claims and has no early prospect of being able to do so;
 - (b) a court of competent authority has made a ruling, for reasons directly related to the financial circumstances of the market intermediary or the financial circumstances of any third party with whom financial instruments have been deposited by the market intermediary, which has the effect of suspending investors' ability to make claims against the firm or the firm's ability to make claims against the third party.
 - (c) Competent Authorities shall determine whether a market intermediary is able to meet its financial obligation as soon as possible and in any event within three (3) months, after first becoming aware that a market intermediary has failed to meet its obligations arising out of investors' claims.

3. The coverage referred to in sub-article 2 shall be provided in accordance with the legal and contractual conditions applicable for claims arising out of a Market Intermediary's inability to perform either of the following:
 - (a) repay money owed to or belonging to investors and held on their behalf in connection with investment business; or
 - (b) return to investors any instruments belonging to them and held, administered or managed on their behalf in connection with investment business.
4. A Competent Authority shall ensure that the funds provide coverage where financial instruments or monies are held, administered or managed for or on behalf of an investor, irrespective of the type of investment business being carried on by the firm and whether or not the firm is acting in accordance with any restriction set out in its authorisation.
5. A scheme shall also provide coverage for CIS unit holders where any of the following conditions is met:
 - (a) the Competent Authority has determined that a depositary or a third party to whom the assets of the CIS are entrusted is unable to meet its obligations to a CIS, for the time being, for reasons directly related to the financial circumstances of the depositary or the third party and has no early prospect of being able to do so; or
 - (b) a Court of Competent jurisdiction has made a ruling, for reasons directly related to the financial circumstances of the depositary or any third party to whom assets of the CIS are entrusted, which has the effect of suspending the CIS ability to make claims against the depositary or the third party.
6. A Competent Authority shall determine within 3 months, after first becoming aware that a depositary or a third party to whom the assets of the CIS are entrusted has failed to meet its obligations arising out of the CIS claims.
7. The coverage for investors in relation to securities business shall be provided in accordance with the legal and contractual conditions applicable for a claim by a CIS unit holder for the loss of value of the CIS unit due to the inability of a market intermediary.
8. A claim shall not be eligible for compensation more than once under this Directive.
9. The amount of an investor's claim shall be calculated in accordance with the legal and contractual conditions, in particular those concerning set off and counterclaims, that are applicable to the assessment, on the date of the determination or ruling.

ARTICLE 6

ADMINISTRATION OF THE FUND

1. The Fund shall be administered by an independent body which shall also be responsible for overseeing compensation.
2. The following may be paid out of the fund:

- (a) money required to be paid as compensation to investors; and
 - (b) any expenses relating to management and investment of the monies constituting the fund.
3. The independent body shall cause proper records in respect of the funds to be kept and shall ensure that:
- (a) the records disclose with reasonable accuracy, the financial position of the fund;
 - (b) the Fund is subjected to an Independent Audit on an annual basis;
 - (c) the records explain in detail all the transactions relating to the fund; and
 - (d) the records shall be kept for a period of seven years.
4. The independent body shall maintain a separate account for the investor compensation fund.

ARTICLE 7

CLAIMS ARISING FROM CRIMINAL ACTIVITY

Claims arising out of transactions connected to a criminal offence or obtained from money laundering or arising out of any other conduct which is prohibited, shall be excluded from compensation.

ARTICLE 8

COVERAGE FOR INVESTOR COMPESATION FUNDS

1. Eligible investors shall be compensated up to US\$1,000 in respect of aggregate claim.
2. The independent body referred to in Article 6 may adjust the amount taking into account the size of the investor compensation fund.
3. The investors listed in Annex 1 shall be excluded from compensation.
4. The compensation limit shall apply to the investor's aggregate claim on the same market intermediary irrespective of the number of accounts, the currency and location within the Community.

ARTICLE 9

FUNDING

1. Competent Authorities shall ensure that the funds have in place adequate measures to compensate investors where need arises.
2. Sources of funds for Investor Compensation Fund shall include;
 - (a) a) such monies that are required to be paid into the compensation fund by Market Intermediaries;
 - (b) b) sums which accrue from interest and returns from investing monies from the investor compensation fund;

- (c) c) such monies recovered by the Competent Authorities from entities which have failed to meet their obligations from investors resulting into payments to the investor compensation fund;
- (d) d) such sums of monies as are paid as fines or penalties under any legislation administered by a Competent Authority;
- (e) e) Such other monies paid as ill-gotten gains where those harmed are not specifically identifiable; and
- (f) f) Such other monies as received for purposes of the Investor Compensation Fund from any other source as determined or approved by the Competent Authorities.

3. The monies shall only be invested in low-risk liquid financial instruments.

ARTICLE 10

PROCEDURES FOR LODGING A CLAIM

1. Where the Competent Authority has appointed a statutory manager it shall inform the Independent body accordingly to oversee the process.
2. The Competent Authority shall immediately upon appointing a statutory manager make an announcement informing the investing public of that appointment and provide contact details of the appointed statutory manager.
3. Where a statutory manager has been appointed, every investor who has suffered a pecuniary loss shall within three (3) months of the announcement notify the statutory manager of such a loss.
4. The statutory manager shall submit to the Independent body a list of investors to be compensated as well as the supporting documents.
5. The Independent body shall verify and approve the claims for compensation payments
6. The statutory manager shall pay all valid claims within six (6) months of its appointment.
7. Where payment has been made out of the compensation fund on behalf of a market intermediary, such a market intermediary shall be liable to the compensation fund for an amount equal to the payment made out of the fund.
8. In the event of liquidation of a market intermediary, the liquidator shall pay the compensation fund any money paid by the fund to investors.

ARTICLE 11

COMPENSATION PAYOUTS

1. The independent body shall take appropriate measures to inform investors of a determination or ruling and, if they are to be compensated, to compensate them as soon as possible.
2. . Every investor who has suffered a pecuniary loss resulting from the failure of a market intermediary to meet his contractual obligations shall apply for compensation to the independent body within three (3) months.

3. In exceptional circumstances, the independent body in consultation with the Competent Authority may extend the time limit.
4. The independent body shall pay compensation within three (3) months of the establishment of the eligibility and amount of the claim.

ARTICLE 12

FAILURE TO CONTRIBUTE

Where a market intermediary is required to contribute to a fund, the Competent Authority shall take all measures appropriate, including the imposition of penalties, to ensure that the Market Intermediary meets its obligations.

ARTICLE 13

INVESTOR COMPENSATION INFORMATION

1. The Competent Authority shall ensure that market intermediaries take appropriate measures to make available to existing and potential investors the information necessary for the identification of the Investor Compensation Fund of which the market intermediary contributes or is a member.
2. The independent body shall inform the public of the rules governing compensation.

ARTICLE 14

SUBROGATION OF RIGHTS

Without prejudice to any other rights which they may have under national law, funds which make payments in order to compensate investors shall have the right of subrogation to the rights of those investors in liquidation proceedings for amounts equal to their payments.

ARTICLE 15

AMENDMENTS

- (1) This Directive may be amended by the Council of Ministers.
- (2) Any proposals for amendment shall be submitted in writing by the Partner States to the Secretary General of the East African Community.

ARTICLE 16

IMPLEMENTATION

- (1) Partner States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive not later than one year from the date of the Council of Ministers' issuance of the Directive.
- (2) The Partner States shall inform the Council of Ministers of the implementation of sub-article 1.
- (3) When Partner States adopt those measures they shall contain a reference to this Directive or shall be accompanied by such a reference on the occasion of their official publication and shall be laid down by Partner States.

ARTICLE 17 ENTRY INTO FORCE

This Directive shall enter into force upon issuance by the Council of Ministers.

ARTICLE 18 ADDRESSEES

This Directive is addressed to the Partner States.

Done in Arusha, Tanzania

ANNEX I

LIST OF EXCLUSIONS

The following investors shall be excluded from compensation:

1. Professional, institutional or qualified investors, including:
 - (a) financial institutions such as banks, insurance companies, savings and credit co-operative societies, micro-finance institutions, credit institutions, forex bureaux;
 - (b) collective investment schemes;
 - (c) pension and retirement funds; and
 - (d) other professional, institutional or qualified investors.
2. Supranational institutions, government and central administrative authorities.
3. Provincial, regional, local and municipal authorities.
4. Directors, managers and personally liable members of a market intermediary, persons holding 5% or more of the capital of such market intermediary, persons responsible for carrying out the statutory audits of market intermediary' accounting documents and investors with similar status in other firms within the same group as such a firm.
5. Close relatives and third parties acting on behalf of the investors referred to in subparagraph 4.
6. Other firms in the same group as the investors specified in paragraphs (1) to (3).
7. Investors who have any responsibility for or have taken advantage of certain facts relating to a market intermediary which gave rise to the firm's financial difficulties or contributed to the deterioration of its financial situation.