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

ANNEXURE IV

PREAMBLE:

The Council of Ministers of the East African Community

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

Having regard to the recommendations of the Sectoral Council on Finance and Economic Affairs;

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 harmonies their financial sector policies and Competent Authority framework 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 harmonize 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 ADOPTED THIS DIRECTIVE.

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ARTICLE 1
INTERPRETATION

For the purposes of this Directive:

1. '**"Market intermediary"** means a broker, dealer, fund manager, investment bank or any other licensed entity by the competent authorities in the EAC Community to provide services in the securities market.

2. **"Investor"** means an individual or a company which uses, has used or is contemplating investing in securities markets through any of the market intermediaries in the EAC Community.

3. '**competent authorities**` means the national regulatory agency that is the primary supervising entity of securities markets in the Partner State.

4. '**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.

5. '**Collective Investment Schemes**' or CIS means schemes as defined in Article 2 of the EAC Directive on Collective Investment Schemes.

6. '**Community**' means the East African Partner States as defined in 7 above.

7. **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.

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 for greater cooperation between investor compensation funds.
(d) To reduce delays in the payout of claims to investors including provision of punitive measures if claims are not settled within a specified period.
(e) To clarify the market intermediaries whose clients should be entitled to compensation under the Investor Compensation Fund Directive

(f) To provide that investors have the right to be compensated by the fund
(g) 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 should 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 independent Competent Authorities enforce the rules consistently, especially as regards the establishment of mandatory compensation funds;
(d) ensure coherence with Partner States' pieces of legislation in this area, as imbalances in information and a lack of transparency may jeopardize the operation of the markets and above all harm consumers and small investors.

ARTICLE 4
SCOPE

This Directive shall apply to all investor compensation funds recognised by the Competent Authorities 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 recognized. Except in the circumstances envisaged in the second subparagraph, no market intermediary authorized in that Partner State may carry on securities business unless it belongs to such fund.

2. A fund shall provide coverage for investors in relation to securities business in accordance with Article 4 where one of the following conditions is met first:

   (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.

Partner States shall ensure that Competent Authorities make the determination referred to in point

(a) of the first subparagraph as soon as possible and in any event within 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 paragraph 2 shall be provided in accordance with the legal and contractual conditions applicable for claims arising out of an 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;

(b) return to investors any instruments belonging to them and held, administered or managed on their behalf in connection with investment business,

Partner States 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 of whether or not the firm is acting in accordance with any restriction set out in its authorisation.

4. A scheme shall also provide coverage for CIS unit holders in accordance with Article 5 where either of the following conditions is met first:

(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;

(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.

Partner States shall ensure that the competent authorities make the determination referred to in point (a) of the first subparagraph as soon as possible and in any event 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.

5. The coverage referred to in paragraph 2 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.

6. No claim shall be eligible for compensation more than once under this Directive.

7. 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 referred to in paragraph 2, of the amount of the money or the value, determined where possible by reference to the market value, of the instruments belonging to the investor which the market intermediary is unable to repay or return.

ARTICLE 6
ADMINISTRATION OF THE FUND

1. The fund shall be admistered by a board of trustees appointed by the Competent Authority which shall also be responsible for overseeing compensation.

2. The Board shall appoint an investment manager(s) who will have full discretion in day-to-day investment management of the portion of the Fund, for which they have been given responsibility, subject to any directions by the Board;

3. The Board shall appoint a Custodian who will be responsible for Custody of the Fund's assets. The appointed custodian shall be one or more financial institutions licensed as a Custodian.

4. The following may be paid out of the fund;-

   Money required by the Competent Authority to pay compensation to investors.
   Any expenses relating to management and investment of the monies constituting the fund

5. The Competent Authority 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
   d) The records required to be kept shall be kept for a period of seven years.

6. The Competent Authority shall maintain a separate account for the Investor Compensation Fund.

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ARTICLE 7
EXCLUSION FOR CLAIMS ARISING FROM CRIMINAL ACTIVITY

Claims arising out of transactions in connection with which a criminal conviction has been obtained for money laundering or arising out of other conduct that is prohibited shall be excluded from any compensation under investor-compensation schemes.

ARTICLE 8
LEVEL OF COVERAGE FOR INVESTOR COMPESATION SCHEMES

1. Partner States shall ensure that schemes provide for coverage of up to US$1,000 for each investor in respect of the claims referred to in Article 2. The Competent Authority may adjust this amount taking into account the size of the investor compensation fund.

2. Partner States which provide for coverage of more than US$1,000 at the time of adoption of this Directive, may maintain that level of coverage for no longer than 3 years from the date for the transposition of this Directive. After that date, those Partner States shall ensure that the level of coverage is up to US$1,000.

3. A Competent Authority may provide that certain investors shall be excluded from coverage by schemes for claims referred to in Article 2 or shall be granted a lower level of coverage. Those exclusions shall be as listed in Annex 1.

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
FINANCING OF INVESTOR COMPENSATION SCHEMES

1. Competent Authorities shall ensure that schemes have in place adequate measures to compensate investors where need arises.

2. Sources of funds for Investor Compensation Fund shall incude;
    a) Market Levies and such other monies which are required to be paid in the compensation fund;
    b) Sums which accrue from interest and profits from investing moneys from the investor compensation fund;
    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) Such sums of money as are paid as fines or penalties under any legislation administered by a competent authority or illgotten gains where those harmed are not specifically identifiable;
    e) 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
COMPENSATION PAYOUTS

1. The Competent Authority or other relevant body shall take appropriate measures to inform investors of a determination or ruling referred to in Article (2) and, if they are to be compensated, to compensate them as soon as possible.

2. It may fix a period during which investors shall be required to submit their claims. That period may not be less than five months from the date of the determination or ruling referred to in Article 2 or from the date on which that determination or ruling is made public.

3. The fact that that period has expired may not be invoked by the fund to deny coverage to an investor who has been unable to assert his right to compensation in time.

4. The Competent Authority or other relevant body shall pay from the compensation fund, an investor's claim not later than three months of the establishment of the eligibility and the amount of the claim.

5. In exceptional circumstances, the Competent Authority may extend the time limit. Any other relevant body responsible for the Investor Compensation Fund may apply to the Competent Authority for an extension of the time limit. No such extension may exceed three months.

6. Partner States shall ensure that compensation funds may participate in insolvency or legal proceedings that may be relevant in establishing the eligibility and the amount of a claim.

7. Subparagraph 6 shall be without prejudice to funds being able to adopt other methods to determine the eligibility or amount of a claim.

ARTICLE 11
PROCEDURES FOR LODGING A CLAIM FOR COMPENSATION

1. Where the Competent Authority has appointed a statutory manager for the purpose of compensation, it shall inform the Board of Trustees 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. Every investor who has suffered a pecuniary loss shall notify the statutory manager appointed by the Competent Authority to handle claims related to the particular market intermediary liable for his loss within three months of the appointment of the statutory manager.

4. The statutory manager shall submit to the Board of Trustees a list of investors to be compensated as well as the supporting documents.

5. The Board of Trustees shall convene a meeting within twenty-one days of receipt of claims for payment by the statutory manager.

6. The Board of Trustees shall verify and approve the claims for compensation payments

7. The statutory manager shall pay all valid claims within six months of its appointment.

8. The statutory manager shall be required to conclude the process of compensation within one year following appointment.

9. 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.

10. In the event of liquidation of a market intermediary, the liquidator shall pay the Compensation Fund any money paid by the Fund to investors on behalf of the insolvent person under these Regulations to the extent of such payment.

ARTICLE 12
FAILURE TO MEET OBLIGATIONS BY A MARKET INTERMEDIARY

1. If a market intermediary required by Article 2(1) to contribute to a fund does not meet its contractual obligations, 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 INFORMATION

1. The Competent Authority shall ensure that market intermediaries takes 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. Investors shall be informed of the provisions of the investor compensation fund, including the amount and scope of the cover offered by the compensation scheme and any rules laid down by the Competent Authority pursuant to Article 2(3). That information shall be made available in a readily comprehensible manner.

3. Information shall also be given on request concerning the conditions governing compensation and the formalities which must be completed to obtain compensation. The information provided shall be fair, clear and not misleading and in particular shall explain the situations and claims covered by the relevant compensation scheme and how it applies in cross border situations. The information provided should also give examples of situations and claims not covered under the fund.

4. The information provided for in paragraph 1 shall be made available in the manner prescribed by national law in the official language or languages of the Partner State.

5. The Competent Authority shall establish rules limiting the use in advertising of the information referred to in paragraph 1 in order to prevent such use from affecting the stability of the financial system or investor confidence. In particular, a Competent Authority may restrict such advertising to a factual reference to the fund to which a market intermediary belongs.

ARTICLE 14
SUBROGATION OF RIGHTS

1. 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.

2. Partner States shall ensure that an investor's right to compensation may be the subject of an action by the investor against the compensation fund.

ARTICLE 15
AMENDMENTS

(1) This Directive may be amended by the Council of Ministers.

(2) Any proposals for amendment may be submitted in writing by the Partner States to the Secretary General of the East African Community.

ARTICLE 16
TRANSPOSITION

(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’ approval. They shall forthwith inform the Council of Ministers thereof.

(2) 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. The methods for making such reference shall be laid down by Partner States.

ARTICLE 17
ENTRY INTO FORCE

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

ARTICLE 18
ADDRESSEES

This Directive is addressed to the Partner States.

Done in Arusha, Tanzania …..

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ANNEX I
LIST OF EXCLUSIONS REFERRED TO IN ARTICLE 8

A Partner State may provide that certain investors shall be excluded from coverage by schemes for claims referred to in Article 2. Those exclusions shall be as listed in Annex 1.

1. Professional and institutional investors, including:

   - financial institutions such as banks, insurance companies, saccos, micro-finance institutions, credit institutions, forex bureaux;

   - collective investment schemes (the entity);

   - pension and retirement funds;

Other professional and institutional 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 point 4.

6. Other firms in the same group.

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.