

EXPLANATORY NOTES TO THE PROPOSED AMENDMENTS TO THE DERIVATIVES RULES

Introduction

In terms of section 116 (3) of the Securities Services Act, 2004 (“the Act”), the JSE is required to “amend or replace” its rules within 6 months of the date of commencement of the Act (1 February 2005), to ensure compliance with the Act. The JSE Rules Working Group (“RWG”) has made amendments to the derivatives rules to the extent necessary to comply with the provisions of the Act.

The derivatives rules will be amended in phases. The primary purpose of the proposed amended derivatives rules published in Phase 1A is to accommodate the introduction of the Act and specifically to ensure compliance with section 18 of the Act. The objective of Phase 1B is to amend the derivatives rules in order to accommodate the proposed membership restructure, which will involve extensive changes to the derivatives rules. JSE Member Notices F668 and A564 of 26 April 2005, set out the proposed membership restructure.

These proposed rules have been drafted on the assumption that the demutualisation amendments, per JSE Member Notices F679 and A571 of 13 May 2005, will be implemented on 1 July 2005.

Consequential changes to the derivatives directives, as a result of the amendments to the derivatives rules, are currently being drafted by the RWG and members will be advised of the draft amended directives in due course.

Section 1 – Derivatives rules

This section remains largely unchanged with the exception of clarification and simplification of some of the rules.

The procedure for amendments to the rules and directives has been altered.

The enabling provisions relating to the Fidelity Fund, which are currently in a separate set of rules, have been included in this section and amendments have been made to the Fidelity Fund Rules. The Fidelity Fund Rules remain separate from the derivatives rules.

Rule 1.40.3, which sets out certain powers of the controlling body of the JSE, has been deleted and this information is now included in the JSE's memorandum of association.

Rule 1.10 has been deleted as provisions relating to the demutualisation of an exchange are set out in the Act and it is not necessary to duplicate them in the rules.

Section 2 – Interpretation and definitions

A number of definitions have been deleted or amended and new definitions have been included as a consequence of the new Act. A new definition, “derivative securities”, has been introduced to distinguish between the wider definition of “securities” in the Act and the securities that are listed by the JSE and traded on the JSE derivatives trading systems.

The definition, “JSE authorised investments”, replaces the definition “other investments” and now encompasses all securities which the JSE will authorise derivatives members to invest in on behalf of their clients. It is also necessary to introduce a definition for “JSE listed securities” in order to distinguish between securities listed on any exchange in the Republic of South Africa and securities listed by the JSE.

Section 3 – Membership and disciplinary procedures

A derivatives member is defined as a category of authorised user. With the implementation of the Act, it is no longer necessary to distinguish between the sub-categories of broking member and non-broking member, consequently these terms have been replaced with “derivatives member”.

The new rule 3.300.1.4 enables a JSE disciplinary tribunal to direct a derivatives member to prevent or relieve an officer or employee of that member from carrying out any specified activity, function or duty for such reasonable period as the JSE disciplinary tribunal deems appropriate.

Section 7 – Trading

A new rule has been inserted which deals with manipulative or deceptive trading practices and introduces the concept of a market corner, which is included in the definitions. A new rule has been inserted to provide for the prohibition on false, misleading or deceptive statements, promises or forecasts.

Section 10 – Sundry provisions

A new rule has been introduced to deal with speculative position limits applicable to the agricultural products market. This rule was previously distributed to members for approval but was never formally approved by the Registrar and hence was never implemented.

Section 11 – Members' and clients' funds

A new rule has been introduced which prohibits members from accepting cash deposits in excess of R5 000. This rule was also previously distributed to members for approval but was never formally approved by the Registrar and hence was never implemented.

Section 15 – Registered officers

Rule 15.60 provides that employees of derivatives members who exercise discretion in the management of JSE authorised investments and/or provide investment advice to clients on the buying and selling of JSE authorised investments must obtain such qualifications as will be prescribed by the JSE in the directives.

The prescribed qualifications will probably be those applicable to junior dealers.

Section 16 – Ethics and conduct

Rule 16.10.1.1 has been amended to provide for the prohibition on the acceptance of inducements by derivatives members, which is contained in the Code of Conduct for Authorised Users published under section 70 of the Act.

Section 17 – Complaints and disputes

The new Act requires the JSE to implement rules relating to complaints received by derivatives members from clients and the resolution of disputes. Derivatives members are therefore required to establish and maintain procedures for the handling of client complaints. This new section also provides for the handling of disputes between a client and a member and between members.

The dispute resolution rules set out the criteria for a complaint to be dealt with in terms of the dispute resolution procedures and the consideration of a dispute by an appointed ombud. These rules replace the previous dispute resolution rules. The JSE's dispute resolution scheme has been drafted in accordance with the provisions of the Financial Services Ombud Schemes Act, 2004, which commenced on 1 April 2005.

Implementation

The amended derivatives rules will be implemented on 1 August 2005.