

Mr Norman Muller
Financial Services Board
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22 June 2011

Dear Norman

RE: CPSS/IOSCO Principles for Financial Market Infrastructures

The consultative report on the Principles for Financial Market Infrastructures which has been prepared by the Committee on Payment and Settlement Systems (CPSS) and the International Organisation of Securities Commissions (IOSCO) has afforded Strate Limited (Strate) an opportunity to review the proposed new standards and principles which may no doubt lead to greater and improved consistency in the functioning, oversight and regulation of financial markets and financial market infrastructures (FMIs). We would like to extend our gratitude and appreciation to the Financial Services Board (FSB) for giving Strate the opportunity to respond to the proposed new principles.

It is the view of Strate that the consultative report, proposed principles and explanatory notes have been written in a very clear and comprehensive manner and we commend CPSS/IOSCO for the work of their technical and working committees who have drafted this report so thoroughly.

Strate's response to the report is attached hereto and provides recommendations to the FSB and IOSCO on each principle where applicable. One worksheet per principle is provided in the attached Excel summary. In addition, while we understand that an Assessment Methodology will be released in time and Strate will be required to formally respond on the extent to which we comply with the final principles, we have taken the opportunity to include a brief list per principle, on the extent to which Strate already aligns with the proposed considerations.

Detailed comments and recommendations are provided in the attached spreadsheet. Some more general comments are noted below:

- Strate understands that the Assessment Methodology will only be released after the final Principles for FMI's has been released and entities will not have an opportunity to comment on the proposed Assessment Methodology. If this is indeed the case, we ask that we please be given an opportunity to review and comment on the proposed Assessment Methodology as has been the approach with the consultative approach with regards to the main Principles.
- In order to avoid undue duplication we recommend that IOSCO should rather cross-reference issues between principles where applicable. The duplication of concepts across multiple principles should be kept to a minimum since this may cause difficulty in complying with one underlying "idea";
- The final principles should align with the explanatory notes in the consultative report which are more general and recognise the alternative structures and models which FMIs may adopt in different jurisdictions. Strate is supportive of IOSCO not being too prescriptive and allowing local regulators and Boards of FMIs to impose specifics as applicable to their markets and structures; and

- Annex C: “*Selected RSSS marketwide recommendations*” should be included /combined into the proposed 24 principles or such principles should be extended to incorporate the important and valid considerations included in this section.

Members of Strate’s executive team will be attending the Global Relations Exchange and Training (GREAT 2011) seminar in New York during July 2011. Mr Jeffery Mooney, Special Counsel, US Securities and Exchange Commission and Co-Chair of the CPSS/IOSCO working committee will be attending and presenting at this seminar. Would the FSB be amenable to Strate sharing our response and recommendations directly with Mr Mooney?

We look forward to receiving the FSB’s response to our recommendations and supporting the final CPSS/IOSCO principles in due course.

Yours sincerely



MONICA SINGER

Chief Executive Officer: Strate Limited.



IOSCO - Principles for Financial Market Infrastructures

Response by Strate Limited.



Key Consideration	Iosco Paper Reference	Comments and Open Items
Principle 1: Legal basis		A robust legal basis for an FMI's activities in all relevant jurisdictions is critical to an FMI's overall soundness. The legal basis defines, or provides the foundation for relevant parties to define, the rights and obligations of the FMI, its participants, and, where relevant, participants' customers. Most risk-management mechanisms are based on assumptions about the manner and time at which these rights and obligations arise through the FMI. Therefore, if risk management is to be sound and effective, the enforceability of rights and obligations relating to an FMI and its risk management should be established with a high degree of certainty. If the legal basis for an FMI's activities and operations is inadequate, uncertain, or opaque, then the FMI, its participants, and their customers may face unintended, uncertain, or unmanageable credit or liquidity risks, which may also create or amplify systemic risks.
		<p>Strate Limited's response on Principle 1.</p> <p>Detail of the extent to which Strate Limited currently complies with, or aligns to, Principle 1.</p>
<p>1. The legal basis should provide a high degree of certainty for each aspect of an FMI's activities in all relevant jurisdictions.</p>	<p>3.1.2 page 19</p>	<p>Strate supports this Principle and Key Considerations.</p> <p>Recommendation to FSB / IOSCO:</p> <p>1. Since the FMI is allowed to carry out other business activities as well that do not bring systemic risk, there is no need to legislate or regulate "each aspect". Cooperation with the regulator is a key factor in deciding what activities of the business must be regulated and what not. Strate is not in favour of restricting CSDs or other FMIs to perform only pre-defined core functions or activities. Markets and market practices continuously develop globally and FMIs should be agile. IOSCO should encourage flexibility in legislation and allow discretion to be given to the regulator to step in when deemed necessary. Over-regulation on each aspect of all activities performed by FMIs would lead to over-regulation and high costs and inefficiencies for investors and others.</p> <p>2. Explanatory Note (EN) 3.1.5 = Needs to be constrained by legal arrangements between FMI's participants and their clients.</p> <p>3. EN 3.1.6 = Duplication with Principle 8 regarding settlement finality should be removed.</p>
<p>2. An FMI should have rules, procedures and contracts that are clear, understandable, and consistent with relevant laws and regulations.</p>	<p>3.1.2 page 20</p>	<p>Strate supports this Principle and Key Considerations.</p> <p>SA legislation prescribes that CSD Rules and Directives must be consistent with laws. This also controlled by regulator in renewal of CSD licence on an annual basis. With regard to procedures and contracts, no legal action has been taken against Strate by its CSD Participants or other third parties since inception. Legal comparisons and compliance on legislation and contracts are done on a regular basis by internal lawyers.</p> <p>SFIDvP enshrined in SSA and CSD Rules. SSA and CSD Rules are available on Strate website. Strate Training division provides training modules on all legal and operational aspects of Strate. Strate Legal's Rule and Directive Setting Process ensures rules and directives are not ultra vires the SSA.</p> <p>Strate strives in all instances to align with global best practices and harmonise rules and procedures with same - for example UNIDROIT on legal issues and ISO15022 standards for messaging.</p>

<p>3. An FMI should be able to articulate the legal basis for its activities to relevant authorities, participants and, where relevant, participants' customers, in a clear and understandable way.</p>	<p>3.1.2 and 4 page 20</p>	<p>Strate supports this Principle and Key Considerations.</p>	<p>SA legislation determines the legal structure and CSD environment is regulated by the FSB. Memoranda of understanding exist between Strate and other SROs (e.g. exchange) and regulatory authorities (e.g. SARB). Legal basis is clear. CSD is SRO. CSD Rules and Directives are binding in terms of SA legislation on CSD Participants and others. Industry standards and market protocols are captured in CSD Directives, where necessary. Proper consultation with market is followed in line with administrative law. CSD Directives are issued to CSD Participants and others. Proper communication channels are in existence and various market committees meet regularly to articulate issues. Authorities have access to all Strate's meetings and documentation.</p> <p>SSA and CSD Rules are available on Strate website. Strate Training division provides training modules on all legal and operational aspects of Strate. Annual SRO Report articulates Strate's regulatory, supervisory and enforcement functions.</p>
<p>4. An FMI should have rules, procedures and contracts that are enforceable in all relevant jurisdictions, even when a participant defaults or becomes insolvent. There should be a high degree of certainty that actions taken under such rules and procedures will not be stayed, voided or reversed.</p>	<p>3.1.4; 3.1.9</p>	<p>Recommendation to FSB / IOSCO:</p> <ol style="list-style-type: none"> 1. Independent legal opinions to interpret enforceability of laws on other jurisdictions must be obtained where necessary. 2. South Africa should sign and ratify Hague Convention to deal with jurisdictional issues more effectively. 3. The UNIDROIT Convention addresses legal consistency and certainty on substantive matters and IOSCO should encourage the ratification of this global standard. The recommendation of these Conventions by IOSCO will speed up the addressing of the specific legal risk. 4. The Principle should be extended to include an FMI's own default. 	<p>CSD Rules, procedures and contracts are enforceable in South African jurisdiction and remain enforceable under SA legislation, even in insolvency. South African CSD Rules, procedures and contracts will only be enforceable in other jurisdictions, if expressly arranged in contracts. To "seek to ensure that activities are consistent with legal basis in all relevant jurisdictions" pre-supposes harmonisation of core legal principles, or express agreement to SA law. Actions taken under CSD Rules etc may be influenced in practice as result of insolvency proceedings. Strate's Participant Failure Manual, Segregated Depository Accounts and new clauses in Financial Markets Bill and Companies Act, 2008 should ensure finality of transactions.</p> <p>Strate Training divisions provides training modules on all legal and operational aspects of Strate. Strate Participant Failure Manual is in place and available on www.strate.co.za.</p> <p>"Choice-of law provisions" would be RSA in terms of Strate Participation.</p> <p>Foreign Participation - RSA jurisdiction is also applicable for issues where Participants are incorporated, located or otherwise conducting business for the purpose of participation outside RSA.</p> <p>Current SSA is silent on insolvency matters and enforceability of CSD Rules against Insolvency Administrators.</p>
<p>5. An FMI conducting business in multiple jurisdictions should identify and mitigate the risks arising from any potential conflicts of laws across jurisdictions.</p>	<p>3.0; 3.1.10 and Principle 20</p>	<p>Recommendation to FSB / IOSCO:</p> <ol style="list-style-type: none"> 1. Strate and other FMIs must cooperate with regulators to create an understanding of the business model in order to make the correct risk analysis. However, regulators should be open-minded to move on according to legislative objectives. 2. Strate agrees that it is necessary to develop CSD Rules and procedures and indicate the law that is intended to apply to each aspect of the FMI's operation. Legal opinions can be obtained to analyse the enforceability of choice of law in relevant jurisdictions. 3. South Africa should sign and ratify the Hague and UNIDROIT Conventions to minimise conflict of laws amongst member states and to minimise the jurisdictional legal risks. 4. IOSCO should encourage the harmonisation of laws and ratification of global standards. IOSCO should require regulators to demand legal opinions on enforceability. 	<p>Legal framework is provided for South African jurisdiction - enforceability of SSA and CSD Rules for foreign Participants is supported by a Letter of Undertaking and Indemnity and confirmed by a legal opinion on the regulated entities jurisdiction.</p> <p>Priority rights were part of Strate's submission to the SSA changes.</p> <p>Strate identifies a possible impact on CSD Links, FundServ and OTC Derivatives projects.</p>

<p>"define rights and obligations of the FMI, its participants and where relevant, customers"; "Therefore, if risk management is to be sound and effective, the enforceability of rights and obligations relating to an FMI and its risk management should be established with a high degree of certainty".</p>	<p>3.1.1; 3.1.5</p>	<p>Recommendation to FSB / IOSCO:</p> <ol style="list-style-type: none"> 1. South African legislation does not define these rights and obligations specifically with regard to insolvency circumstances. The proposed FM Act would need to do this. 2. UNIDROIT specifically defines rights and obligations, also in insolvency circumstances. IOSCO should adopt the core rights and obligations as set out in UNIDROIT as a global standard across jurisdictions. 3. The legal risk cannot be seen in isolation, and credit risk also plays a huge role here. 4. Ensure UNIDROIT principles with regard to rights and obligations of all intermediaries are contained in new FM Act, including the ones on insolvency. 	<p><i>Obligations of intermediaries have become more onerous in the last decade. It is important for the industry that the rights of stakeholders are also taken into account. SA legislation defines rights and obligations in general.</i></p>
<p>"A TR's rules, procedures and contracts should be clear as to the legal status of the transaction records that it stores"; "A TR should identify and mitigate any legal risks associated with any such ancillary services that it may provide";</p>	<p>3.1.3 Principle 24</p>	<p>Recommendation to FSB / IOSCO:</p> <ol style="list-style-type: none"> 1. CSDs should be able act as TRs and are doing so currently in most countries. 2. IOSCO should be clear on what is expected where CSDs and other FMIs fulfill this role. 	<p><i>Strate has an information storage policy and compliance is monitored.</i></p>
<p>"the legal basis should also set out the rules and procedures for providing access and disclosing data to participants, relevant authorities, and the public to meet their respective information needs, as well as data protection and confidentiality issues"</p>	<p>3.1.3 Principle 24</p>	<p>Strate supports this Principle and Key Considerations.</p>	<p><i>SA legislation prescribes.</i></p>
<p>"The legal basis should fully protect from the insolvency of relevant parties and other relevant risks a participant's assets held in custody by the FMI, as well as an FMI's assets held at a custodian or linked FMI"; "the legal basis should provide certainty of rights and interests covering, where applicable, an FMIs interests in and rights to use and dispose of collateral, to transfer ownership rights ... and to make and receive payments, notwithstanding ...insolvency of its participants, participants' customers, or custodian bank."</p>	<p>3.1.5 Principle 11 on CSDs and 14 on segregation</p>	<p>□□</p> <p>Recommendation to FSB / IOSCO:</p> <ol style="list-style-type: none"> 1. Segregation of securities should be prescribed at all layers of the holding chain and up to the level of beneficial holder. 2. IOSCO should recommend how segregation should be done in practice on accounts for each beneficial shareholder and how this should be done in the case of nominees and omnibus accounts. 	<p><i>SA legislation prescribes. Securities are ring-fenced.</i></p>

<p>For TRs ...rights of participants and others with respect to data stored in the TR's systems"</p>	<p>3.1.5 Principle 24</p>	<p>Recommendation to FSB / IOSCO:</p> <p>1. Data warehousing can also be done by CSDs. IOSCO should recognise role that CSDs can play in data storage for governments, tax authorities and other authorities.</p> <p>2. Not all forms of data have same legal value or standing. IOSCO should distinguish carefully classes of data and not encourage the over-regulation of all data bases.</p>	<p>SA legislation prescribes the provision of data to relevant authorities via CSDs and Exchanges. Confidentiality issues are prescribed in law. Data contained in messages embody certain legal rights and interests, such as ownership.</p>
<p>On settlement finality: point which transactions are irrevocable, also in insolvency</p>	<p>3.1.6</p>	<p>□□</p> <p>Recommendation to FSB / IOSCO:</p> <p>1. It is very important that finality can only be revoked under very specific circumstances. The balance needs to be defined between the finality of a transaction and the very exceptional circumstances when the transaction may be revoked, e.g. by court order or not. IOSCO should encourage UNIDROIT principles to be incorporated in all jurisdictions. IOSCO should provide basis for defining exceptions to general rule of finality.</p>	<p>Current SA legislation does not sufficiently deal with finality in insolvency circumstances. Insolvency Act (s 35A and 35B) that also delegates power to CSD to issue certain rules, has only limited applicability and is not sufficient. New FM Act should address issue. Proposed FM Act should capture concept carefully as submitted by Strate. The Companies Act, 2008 now also refers to irrevocability in the case of insolvency.</p>
<p>On settlement finality: cash leg</p>	<p>3.1.6</p>	<p>Strate supports this Principle and Key Considerations.</p>	<p>Strate only settles in central bank money. SA Legislation on national payment system is clear and supports delivery versus payment.</p>
<p>On netting arrangements: enforceability of arrangement in law; also when FMI or its participants are insolvent.</p>	<p>3.1.7</p>	<p>□□</p> <p>Recommendation to FSB / IOSCO:</p> <p>1. Enforceability of netting arrangements should be addressed / considered where two or multiple jurisdictions are involved to avoid possible risk, even systemic risk. IOSCO should also recognise this as a technique to reduce counterparty risk.</p> <p>2. IOSCO is not clear on the preferred method to reduce exposure to the insolvency of a counterparty. Does it recommend netting or the use of collateral in a form of security interest (pledge/out and out cession/hypothec, etc)? Or both? What is the view of IOSCO on prefunded default arrangements?</p> <p>3. IOSCO should specifically address "cherry picking" powers of insolvency administrators.</p> <p>4. IOSCO should support the proper operation of netting agreements. UNIDROIT is currently doing a study on this topic ("Netting of Financial instruments study 78C") and IOSCO should be made aware of this.</p>	<p>Netting is a new concept in many jurisdictions. In SA, it is recognised under Insolvency Act s 35A and 35B, but not expressly recognised in other SA legislation. The enforceability of the netting arrangement of another country should be clear. Proposed FM Act should expressly allow for netting arrangements and fill the legal gaps of the s 35A and 35 B provisions.</p>

For CCPs, state when and under what circumstances novation or off-setting may be revoked even after the acceptance of a trade, otherwise netted amounts may not accurately represent the obligations of the relevant parties.	3.1.8	Same as above	
On enforceability: "Insolvency law should support isolating risk and retaining and using collateral and cash payments previously paid into an FMI, notwithstanding the default or insolvency"	3.1.9	Strate supports this Principle and Key Considerations.	<i>NPS Act; s 35A and B of Insolvency Act. Cash in fungible pool.</i>
"in extreme circumstances, restrict access or not perform the problematic activity until the legal situation is addressed"	3.1.11	Recommendation to FSB / IOSCO: 1. Legal situation may also be addressed by better supervision and surveillance methods.	<i>SA legislation makes provision for suspension and determination and further legal action to be taken by the regulator against the CSD or exchange.</i>