

# SEGREGATED DEPOSITORY ACCOUNTS FAQ



[www.strate.co.za](http://www.strate.co.za)

*strate* 

South Africa's Central Securities Depository



## 1. What is a Segregated Depository Account (SDA)?

'Segregated Depository Account' (SDA) means a designated Central Securities Account opened in the name of a Client, administered by a Central Securities Depository (CSD) Participant and clearly segregated and distinguishable from the Participant's Central Securities Account. This account is held at the CSD.

## 2. What is the purpose of an SDA?

The key purpose of an SDA is to provide a safe-keeping account structure for Investors ahead of any Insolvency Proceeding being instituted against their chosen Participant with full legal ownership remaining undisturbed. The product is designed to reduce market, price and operational risk by avoiding a situation where the Securities may otherwise have been trapped in the books of the failed Participant while the Insolvency Administrator endeavours to identify their ownership and return the Securities to the rightful owner.

The SDA functionality significantly enhances the portability of a clients holdings, allowing them to engage with an alternate service provider at short notice thereby ensuring that if there was an Insolvency Proceeding instigated against their Participant, their account would not be frozen by the Insolvency Administrator and the Client could continue trading in that account in a relatively seamless manner.

## 3. Why has South Africa introduced the SDA concept?

The inter-dependence of the world's financial markets took centre stage with the failure of Lehman Brothers in September 2008. As the significance of this event has rippled through the financial world, many financial institutions and Investors are calling for higher levels of transparency, increased regulation and improved access to their Securities in the event of an intermediary failure.

An international trend has recently developed whereby Clients are becoming more insistent on having their Securities safe keeping accounts opened directly in the books of the CSD in order to further protect themselves in the event of an Insolvency Proceeding being instituted against their chosen Custodian or Participant in the local market. In addition, it is also widely acknowledged that a safe



and efficient CSD promotes the efficient and effective management of risk through the centralisation of specific activities. The maintenance of SDAs is seen as one of these activities whereby the record-keeping function lies with a truly independent third party.

## 4. What are the benefits of an SDA?

SDAs offer numerous benefits to Clients and Investors, including:

- The option of opening a direct SDA at the CSD as opposed to remaining in a Sub-register holding chain in the name of a CSD Participant Nominee;
- Clients/Investors who select the option, through their CSD Participant, to open an SDA directly with the CSD, have the legal security and protection of their Securities in the case of an Insolvency Proceeding against their CSD Participant, thereby reducing both operational and systemic risks;
- In the event of an Insolvency Proceeding, this product is designed to reduce market, price and operational risk by avoiding a situation where the Securities may otherwise have been trapped in the books of the failed Participant, while the Insolvency Administrator endeavors to identify their ownership and return the Securities to the rightful owner;
- The SDA functionality significantly enhances the portability of Clients holdings, allowing them to engage with an alternate service provider at short notice thereby ensuring that if there was an Insolvency Proceeding instigated against their Participant, their account would not be frozen by the Insolvency Administrator and the Client could continue trading in that account in a relatively seamless manner; and
- The ability to appoint a Primary and Secondary Participant where, in the event of Insolvency Proceedings being instituted against the Primary Participant, the custody and administration of the Client's Securities can be switched to their appointed Secondary Participant almost immediately. This has the effect of significantly reducing the risks associated with time delays and other operational impacts while having to move a portfolio from one Participant to another.



## 5. What is a Primary and Secondary Participant?

A 'Primary Participant' is the Participant responsible for administering an SDA on behalf of a Client / Investor. Clients / Investors may appoint a Secondary Participant upfront when opening an SDA account. In the event of an Insolvency Proceeding being instituted against such Primary Participant, the Client / Investors account would be switched to the Secondary Participant.

Therefore a 'Secondary Participant' means the Participant appointed by a Client to administer an SDA in the event of an Insolvency Proceeding being instituted against their Primary Participant.

## 6. Who can open an SDA?

Any Client / Investors of a broker or Participant may open an SDA via their Participant. SDA's are available to both local and foreign investors.

## 7. How does one open an SDA?

Equities:

Upon receipt of the completed Account Opening Form from both the Primary Participant and Secondary Participant (where applicable), Strate will, on behalf of a Primary Participant:

- Open a Segregated Depository Account; or
- Designate an existing Central Securities Account as a Segregated Depository Account.

Within 48 hours, Strate will notify the Primary Participant in writing that a Segregated Depository Account has been opened and the account number thereof as well as notify the Secondary Participant appointed, where applicable, that a Segregated Depository Account has been opened.

Bonds:

Upon receipt of the completed Account Opening Form from both the Primary and Secondary Participant (where applicable), Strate will authorise the Primary Participant to open a Segregated Depository Account in the CSD System.



The Primary Participant must notify Strate in writing that a Segregated Depository Account has been opened, and the account number thereof. Strate will notify the Secondary Participant appointed, where applicable, that a Segregated Depository Account has been opened.

## **8. Do all SDA Clients/ Investors need to appoint a Secondary Participant upfront?**

No, a Client/ Investor may appoint a Secondary Participant either upfront when they open an SDA or at a later stage. The details of the appointment are provided to Strate via the Primary Participant as well as by the Secondary Participant.

The Primary and Secondary Participants are responsible for entering into or amending a Safe Custody Agreement / Client Mandate with the Client / Investor and all standing instructions will be communicated and switched to the nominated Secondary Participant in the event of the Primary Participant failing.

## **9. What happens if a Client does not appoint a Secondary Participant upfront?**

If the Client has not appointed a Secondary Participant upfront this could lead to time delays associated with the completion and confirmation of the required documentation. It could also result in the delay to the transferring of Securities from the Primary Participant to the Secondary Participant in the event of Insolvency Proceedings being instigated and thereby restricting the Clients access to their own securities.

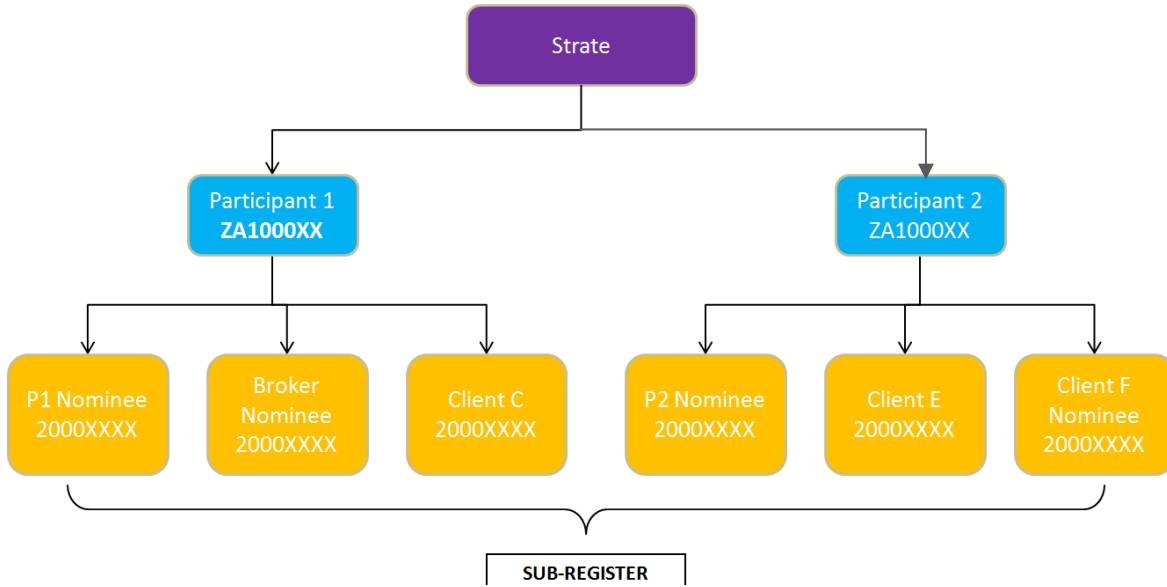
## **10. What legal standing does an SDA have?**

The Companies Act, 2008 (Act 71 of 2008) (effective May 2011) enabled Strate to revise its CSD Rules to allow legal record of ownership to be recorded at the CSD. By allowing Clients' SDAs to be opened directly in the books of the CSD, Investors are granted full legal ownership rights upon credit of their accounts, providing legal certainty to them at all times. While Clients' Securities held in Participants' nominee accounts will not fall in the intermediary's estate upon occurrence of an Insolvency Proceeding (see specifically section 40(2)(a) of the Securities Services Act (Act 36 of 2004)), the proposed SDAs guarantee full legal ownership and immediate direct access at CSD level.

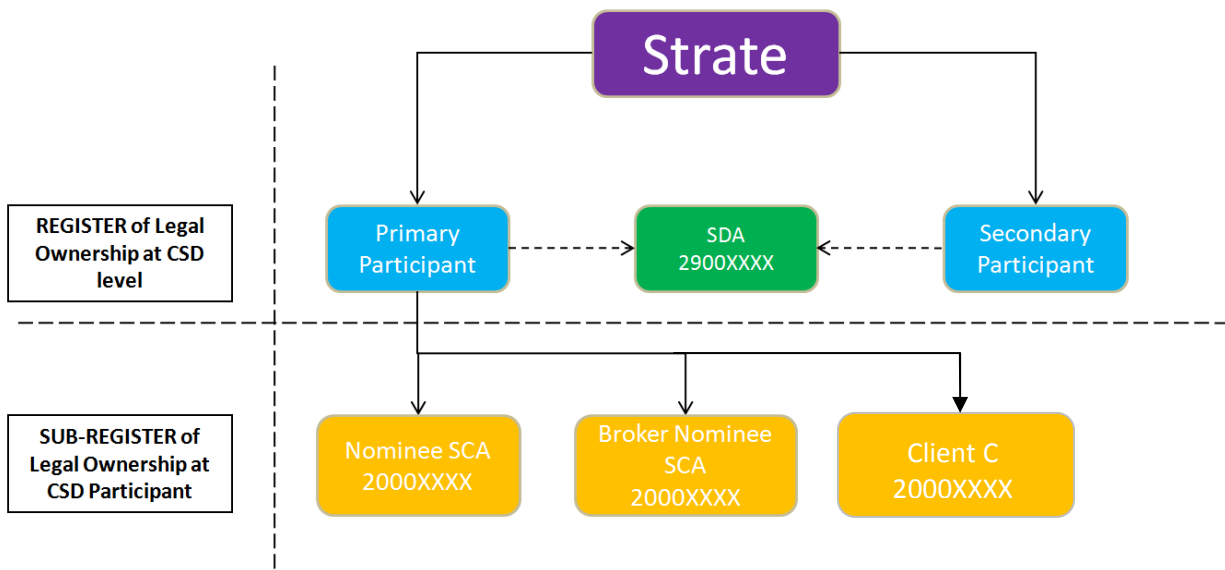


## 11. How does the SDA structure differ from the current custody account structure?

The current account structure appears as follows:



The SDA structure is as follows:





## 12. Which markets are the SDA applicable to?

The SDA concept is only applicable to the Equities and Bonds markets. Money Markets has an SOR account structure and therefore the record of ownership sits in the books of the CSD / Strate.

## 13. Who operates the SDA on behalf of the Client?

SDAs will be operated by the Participant in the same manner as any other Central Securities Accounts held at the CSD.

## 14. How is an SDA different to the proposed Securities Ownership Register (SOR) model in South Africa?

The SDA model is not the same as the proposed Securities Ownership Register (SOR) model in South Africa for the following reasons:

Segregated Depository Account (SDA)	Securities Ownership Register (SOR)
None transparent holding structure (nominees allowed)	Transparent holding structure
Fragmented holding structure (registers)	Centralised holding system
Indirect relationships with Issuer (where nominees are used)	Direct relationship with Issuer
Caters for Secondary Participant upon Insolvency Proceedings	Does not cater for Secondary Participant upon Insolvency Proceedings
No change to settlement procedures	Possible change to settlement procedures
No change to corporate action procedures	Possible change to corporate action procedures
Client mandate signed with both Primary and Secondary Participant	Client mandate signed with only the current Participant
Mitigates risks surrounding Insolvency Proceedings against a Participant	Possible risk mitigation opportunities



## 15. Can an entity open an SDA if they are a Nominee?

Yes, Nominees may choose to open an SDA. There are no additional Nominees requirements under the SDA structure other than those that already apply in the Strate environment.

The current Strate Nominees requirements, which therefore also apply to SDA's are:

- 1) Local Nominee
  - a. If entity is a Broker – approved by the JSE;
  - b. If entity is a Participant – approved by Strate;
  - c. If entity is Client of a Broker – approved by FSB;
  - d. If entity is a Client of a Participant – approved by FSB and Strate.
- 2) Foreign Nominee
  - a. The entity must provide proof to their Participant from their Regulator that they are permitted in their jurisdiction to operate a nominee in South Africa.

## 16. What risks are mitigated through an SDA?

There are numerous risks which are mitigated by an SDA. These include the market, price and operational risk by avoiding a situation where the Securities may otherwise have been trapped in the books of the failed Participant while the Insolvency Administrator endeavors to identify their ownership and return the Securities to the rightful owner (as well as the mitigation of liquidity and settlement risk under such circumstances.) Naturally legal risk is also better managed by providing full legal ownership rights and legal certainty of ownership to Investors. The SDA functionality significantly enhances the portability of client's holdings, allowing them to engage with an alternative services provider at short notice.

## 17. When will the project be implemented?

A Proof of Concept (POC) phase of the project has been implemented as of September 2011 and is anticipated to run for a period of nine months during which time this product will be available to selected Participant Clients / Investors.



## 18. Is there a cost involved?

Yes, the Strate fee for an Equities and Bonds SDA is R 500.00 per month, per SDA, during the POC phase. The fee will be reviewed after this phase is complete.

## About Strate

Strate Limited (Strate) is the licensed Central Depository (CSD) and a Self-Regulatory Organisation (SRO) in South Africa in terms of the Securities Services Act, 2004 (SSA). To fulfill its legislative SRO requirements, Strate supervises compliance by Participants with the SSA, the Strate Rules and Directives. This effectively means that Strate regulates the custody and settlement operations of the Participants.

Strate's core purpose is to mitigate risk, bring efficiencies to South Africa's financial markets and improve its profile as an investment destination. Strate is aligned to international best practices and continually strives to ensure operational excellence and provide enhancements for the good of the Southern Africa financial markets. Strate handles the settlement of a number of Securities including equities and bonds for the Johannesburg Stock Exchange (JSE) as well as the range of derivative products such as warrants, Exchange Traded Funds (ETFs) retail notes and tracker funds. It has now added the settlement of money market to its portfolio of services. It provides services to Issuers for their Investors in terms of the Companies Act and Securities Services Act.

Additional information may be found at [www.strate.co.za](http://www.strate.co.za) | Twitter:@strateltd | YouTube:

[www.youtube.com/user/StrateLtdCSD](http://www.youtube.com/user/StrateLtdCSD) | Facebook: <http://www.facebook.com/#!/groups/107241797726/>

| LinkedIn: <http://za.linkedin.com/pub/strate-ltd/22/1b/195>