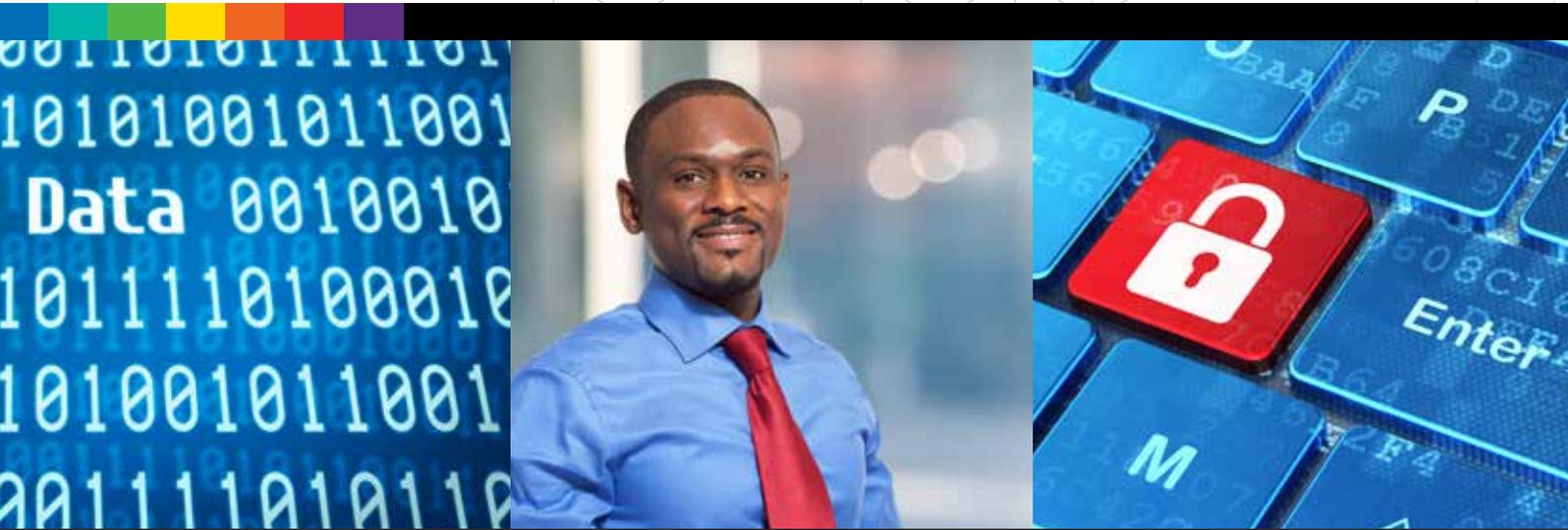




# Debt Instruments Solution (DIS)

*Issuer Guide to DIS*



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## Introduction

In the second quarter of 2017, Strate is planning on implementing its Debt Instrument Solution (DIS) project. The aim of this project is a replacement of the current UNEXcor system, which has been operational since 1991, with world-class technology in line with Strate's IT roadmap. This will improve on many facets of the value chain in the post-trade space by revolutionising the bonds settlement model, as well as bonds capital events processing.

## Purpose of the Document

This document is aimed specifically at the role of the Issuer within the bonds market. These interactions start from the creation of the Issuer's Programme Memorandum to the listing of specific Financial Instruments under such a Programme. They further include the servicing of any coupon and capital repayments associated with such issues. There are significant changes to the bonds settlements model and the account structures within Strate, the Central Securities Depository. However, this document will focus on the interactions between the Issuer and Strate. The document aims to also highlight the improved communication and processing of security details and the confirmation and payment of entitlements, through the relevant downstream stakeholders to the underlying noteholders.

As there are no changes to the process with regard to the approval of an Issuer and the Programme Memorandum, the document will introduce new roles within the system and define how these applicable roles will interact with Strate and

highlight the applicable areas that will impact Issuers, either from a system or from a business process perspective. Thereafter, it will focus on highlighting the changes to the following main areas, firstly the Issuing of a Financial Instrument (ISIN is the unique number that is assigned by the National Numbering Agency to identify a Financial Instrument), secondly the process around confirmation of coupon and partial redemptions amounts to be disbursed (*Please note that full redemption proceeds as a bullet on redemption date will not have to be confirmed by the Issuer prior to payment date*) and thirdly, the payments of coupon and redemption amounts to be distributed.

In development of the Bonds DIS Project's Business Requirements Specifications (BRS), which was signed off by Market Participants in 2012, contributors endeavoured to synergise between the Money Market and the Debt Instrument Market with the intention of limiting the amount of re-work necessary for both Strate and its Clients.

## Defining the New Roles

For purposes of the Strate system, we distinguish between the role of an Issuer and an Issuer Agent. Please note that this distinction is of vital importance as it will be the deciding factor on how an Issuer chooses to interact with Strate. The objective is to minimise the inefficient and time consuming manual processes that currently exist between Strate, Issuers and CSD Participants, which ultimately impact on efficiencies through to noteholders. By leveraging off the Money Market infrastructure that exists, high levels of Straight-Through-Processing (STP) can be achieved utilising the existing processes in place with many Issuer Agents currently common across both the Money Market platform and the Bonds platform.

***We will now focus on the three impacted areas:***

### 1. Listing Process (ISIN Issuance)

There are no changes to the current process with regards to the interaction with the JSE. The Issuer will continue to comply with the existing processes of obtaining an ISIN from the JSE subject to the normal requirements in terms of the current JSE Listings Requirements.

For the Primary Issuance, the Issuer will no longer be required to complete the “Instructions For The Electronic Capture of Uncertificated Securities”

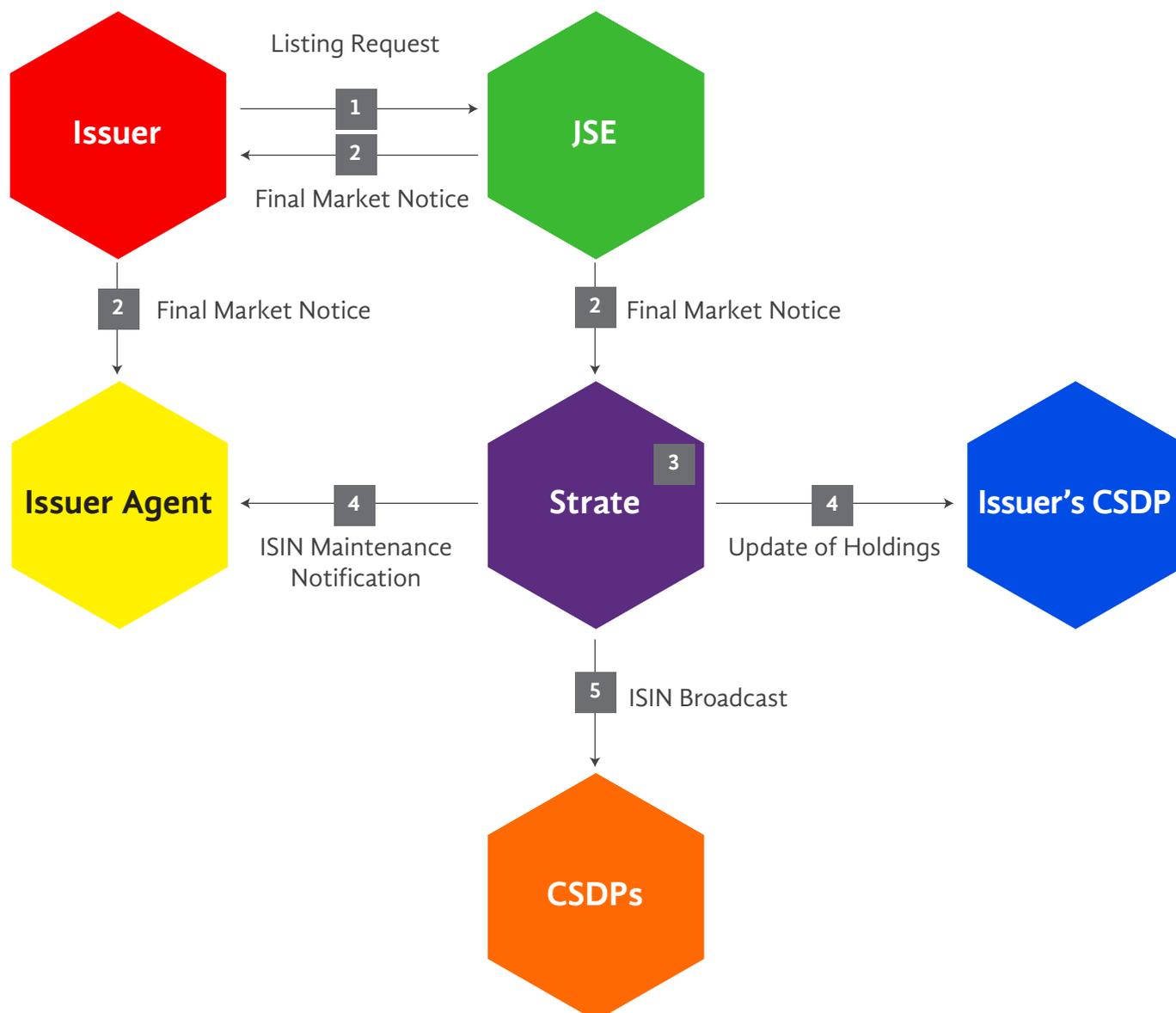
A ‘Direct’ Business Partner is an institution or individual that is electronically connected to the Debt Instrument System with access ‘rights’ in accordance with their Debt Instrument System ‘role’. In the DIS solution, an Issuer Agent is a Direct Business Partner.

An ‘Indirect’ Business Partner is an institution or individual that is not electronically connected to the Debt Instrument System; and will not directly interact with the Debt Instrument System, but will appoint a ‘Direct’ Business Partner to act on their behalf. In the DIS solution, an Issuer is an Indirect Business Partner. An Issuer may appoint themselves as an Issuer Agent.

top-up form currently in place. The Issued Amount will form part of the Final Market Notice and will be automatically updated on Issue Date.

This process is detailed below and explains the interaction that takes place amongst all the market Participants to ensure that the correct securities information is uniformly communicated and stored.

## Listing Process



1. The Issuer will submit all the Listings documentation, per the JSE Listings Requirements and the current process, to the JSE.
2. The JSE will generate a Final Market Notice and send it to Strate and the Issuer. This will contain the ISIN salient details.
3. Strate will create the ISIN details as per the Final Market Notice and the details will be stored in Strate's Securities Register. The Issued Amount will be updated on Issue Date.
4. Strate will advise the Issuer's CSD Participant as well as the Issuer Agent of the security details and an update to the holdings. The Issued Amount will be electronically updated.
5. Strate will advise all CSD Participants of the creation of a new Security.

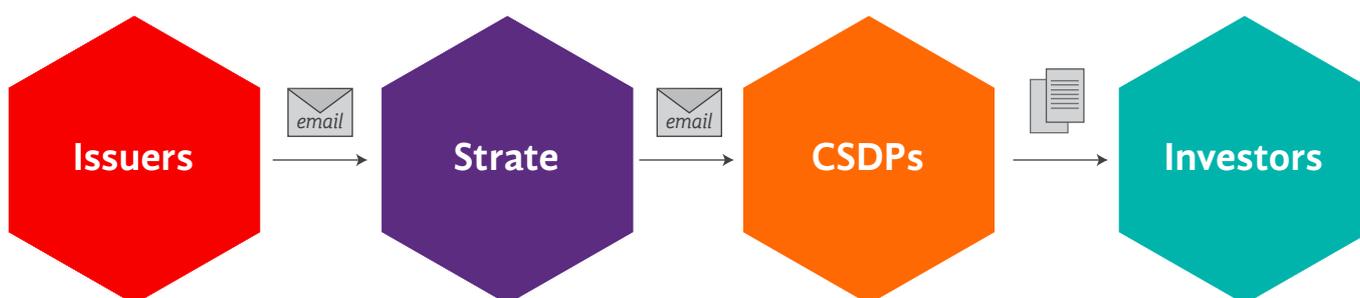
## 2. Coupon and Partial Redemption Confirmation Process

### Current Manual “Communication of Entitlement” Process

Currently, the Strate Operations team extract all upcoming coupon events based on last day to register (LDR). They then communicate via e-mail requesting that the Issuer/Calculation Agent confirm the details of the upcoming payment (i.e. Amount of the coupon to be paid over to Strate on Payment Date based on the coupon period as well as the applicable rate for the said coupon period). Strate, in turn, manually collates all of the information for a particular Payment Date and this

information is communicated via e-mail to CSD Participants who are holders of the applicable security that is due for payment.

The same process is followed in connection with Asset Backed Securities (ABS), where the capital is redeemed along with the coupon payment on the scheduled coupon payment dates over the life of the security – these dates are not catered for in the UNEXCOR system.



*Communication of Entitlement (current process)*

Strate has numerous concerns regarding the obvious inefficiencies associated with the current confirmation of entitlements process, such as:

- Privileged and confidential information is sent via email and consequently people could inadvertently fall foul of POPI (Protection of Personal Information Act) regulations.
- There is no structure with regard to how the information is communicated downstream, as we are dependent on receipt of the information from Issuers. This information is received at different times and consequently communicated haphazardly to CSD Participants.
- The process is manually intensive - which impacts on cost, quality and time taken for information to be distributed. We have seen the benefits of automation in the electronic Money Market product in that confirmations are received within seconds of being sent to Issuer Agents.
- Increased risk of error as a result of the manual work required from various teams in the chain.
- The process is archaic in relation to global standards and processes.

Due to these concerns, the emails will be replaced by utilising SWIFT messages and leveraging off standards that have already been developed in the market.

## New automated “Communication of Entitlement” Process

An Issuer appoints an Issuer Agent, which is an institution that acts on behalf of the Issuer of securities. An Issuer Agent is a role within the Strate system that communicates directly with the CSD. An Issuer may elect to be their own Issuer Agent.

There is a Securities Register within the CSD system. This register contains all the ISIN attributes. From the setup of the ISIN attributes, within the system, the coupon payment dates as well as partial and full redemption dates can be anticipated at the time of creation on Issue Date.

The system is built to cater for four specific types of instruments:

- 1.) Discounted notes
- 2.) Fixed rate notes with a fixed redemption date
- 3.) Variable rate between coupon periods with a fixed redemption date (Typically JIBAR linked notes) and
4. Other typically Asset Backed Securities or securities where the coupon rate is determined based on the performance of an underlying factor.

The computation for coupon payments in the category 2 and 3 categories are fairly simple and the value Strate adds is that it anticipates these amounts due by the Issuer. The Issuer is simply required to confirm such amount or override it to pay what they want. For category 4 instruments the Issuer would

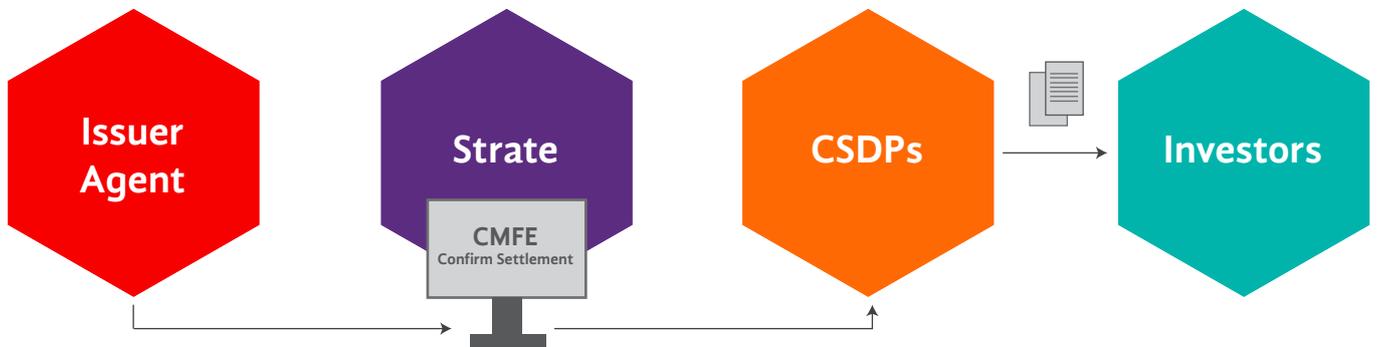
merely provide the amount to be paid for the coupon.

Emails will be replaced and Issuers will be required to communicate these entitlements electronically with Strate. Issuers can either be their own agent or they can appoint an Issuer Agent in order to facilitate this entitlement confirmation process.

Strate will be providing a system that caters for an Issuer Agent Interface to the new Bonds System. This system is called the Central Messaging Front-End system (CMFE) and this will be an option for an Issuer Agent to interact with Strate directly. CMFE for Bonds is being developed and tested and more details will be provided in due course.

Alternatively an Issuer Agent may elect to communicate via SWIFT directly with Strate via their own systems, which would synchronise with Strate’s Debt Instrument Market system (many existing Issuer Agents currently have this functionality already developed within their environments. They are successfully utilising it in the electronic dematerialised Money Market product offered by Strate, where confirmations are electronically received within seconds). These systems provide improved communication between Issuers and Strate, and ensure the reduction of errors, as well as the timeous communication of entitlements.

## Option 1 - Central Messaging Front-End System

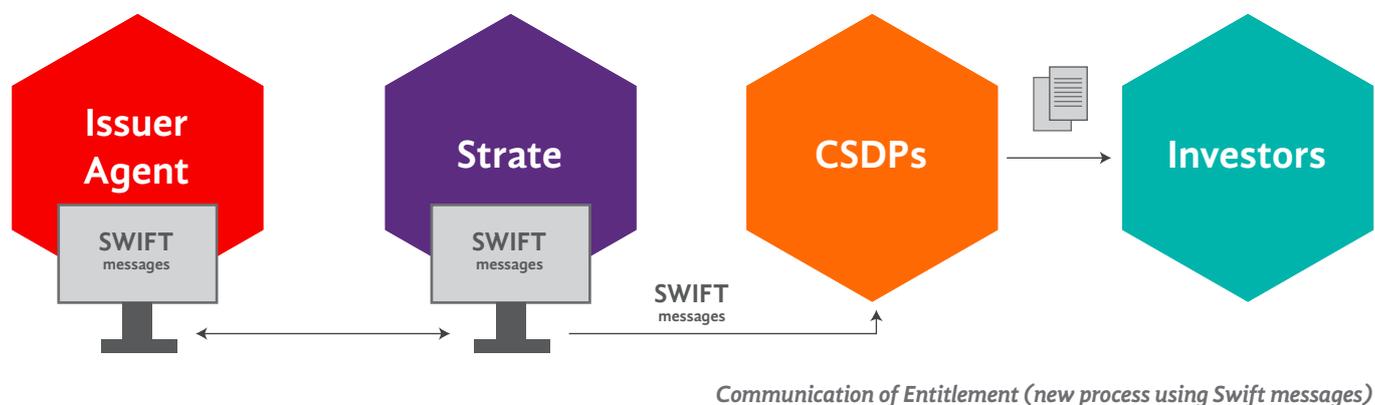


*Communication of Entitlement (new process using Strate's Central Messaging Front-End System)*

Strate has implemented the CMFE system for those Issuers who do not have an existing Issuer Agent system (which integrates with Strate), or who do not wish to expend resources, time or expense in developing an in-house system to interface with Strate. The CMFE is an ideal solution, as it is an internet-based application that is cost effective (No installation is required). This system is currently being developed and tested and further details will be provided with regards to installation, training and costs. The CMFE system provides a single-source, simple and user-friendly user interface with which Issuers can effectively communicate entitlements with Strate.

This simply means that should an Issuer have an upcoming coupon payment instead of sending an email to Strate they simply log on to an application and confirm the upcoming entitlement via this application. If you have not appointed an Issuer Agent who has such connectivity to Strate, and you wish to activate the use of the CMFE yourself, kindly contact [StevenI@strate.co.za](mailto:StevenI@strate.co.za) for more information.

## Option 2 - Debt Instrument System



In this option, the possibility for automation on the side of the Issuer Agent improves greatly. In this scenario, the Issuer Agent would typically act on behalf of numerous Issuers. Many issues of Issuer`s have common payment dates and the consequence is that Issuer Agents confirm multiple coupon payments on a daily basis (with volume spikes particularly around the March, June, September and December quarters).

What this entails is a level of automation from Strate to the Issuer Agent. We would communicate via SWIFT, which the Issuer Agent would be able to validate against their own systems calculations and confirm automatically once matched.

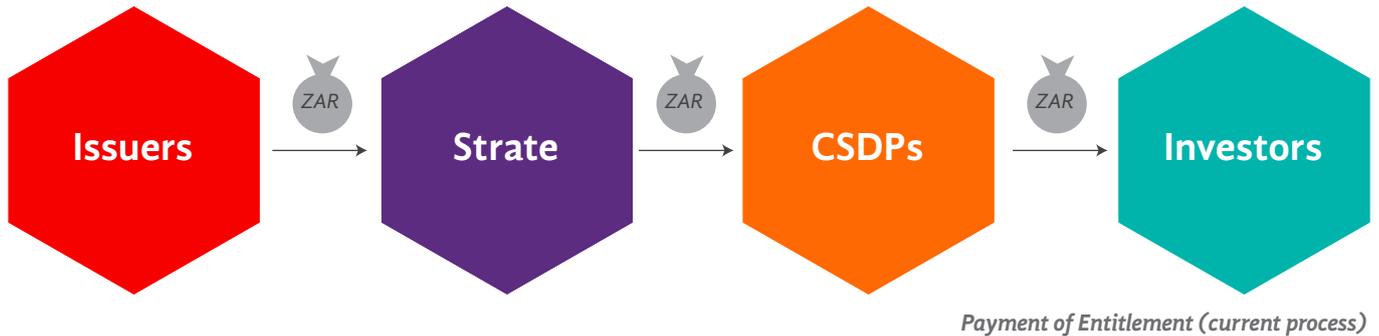
This model has the advantage in that the process is currently been followed in the electronic Money Market space and the levels of automation are evident in that we are receiving confirmations from Issuer Agents within seconds of the message for confirmation being generated by Strate. Many of the existing Issuer Agents are common with the Issuer Agents who are operating in the Bond market. Thus, we are aware that this architecture exists within these entities – it then becomes a question of synergy and rolling this out to the necessary parties that are operating on the Bond market and merely adjusting the business process around confirmations from the manually intensive email process currently in place.

### 3. Payment Process

Currently, proceeds for Capital Events are paid into the account of the commercial bank that Strate holds an account with. These funds are then in turn

paid out by Strate to the CSD Participants who in turn pay to the underlying noteholder.

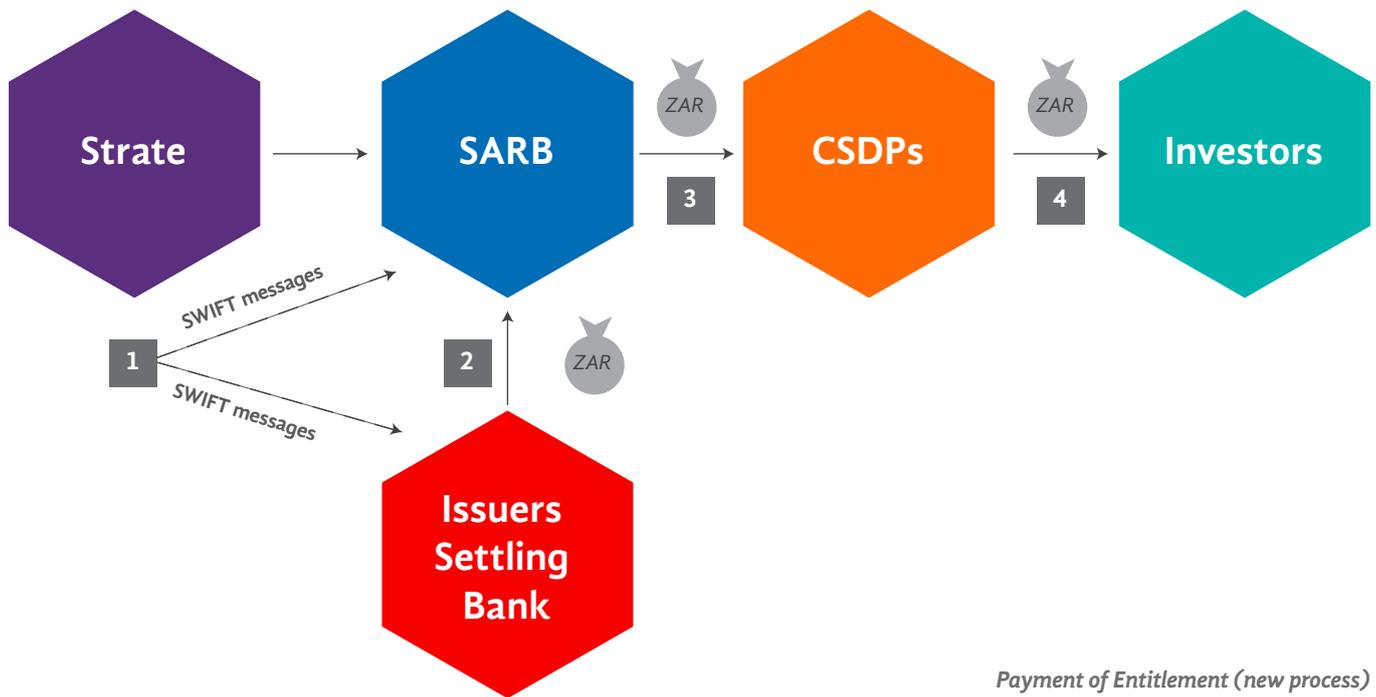
#### Current Manual 'Payment of Entitlement' Process



Strate has concerns regarding the current processing of entitlements, such as:

- The additional step introduces an unnecessary risk into the process via commercial bank funds of the CSD.
- This step introduces an unnecessary leg into the funding requirement which, as a consequence, leads to a delay in the time that funds are received by Investors.
- In the Bonds environment, Strate undertook an exercise to transform from an immobilised environment to a fully dematerialised environment. As a consequence, "CD Nominees" is no longer reflected as the registered holder of notes and there is no requirement to fund the CD Nominee account.

## Automated 'Payment of Entitlement' Process



Payment of Entitlement (new process)

In the new model, there is no need for the Issuer to fund the account of the commercial bank of Strate by 10h00 on Payment Date.

*NOTE: The Issuer must sign an agreement appointing their Settling Bank, who will be responsible for the payment of the coupon and/or redemption on Payment Date. This agreement must be provided to Strate for purposes of recoding the Settling Bank associated with every Issuer. The Settling Bank is a Direct Participant in the Strate system. We are asking all issuers to conclude this agreement and advise Strate of this arrangement on or before end January 2017.*

The Issuer must fund the account at the Settling Bank and instruct the Bank to act on Strate's funding request.

On Payment Date, Strate will send a payment request to the appointed Settling Bank advising what the funding obligation is (For coupon and partial capital redemptions, this is based on the confirmation of the Issuer Agent whilst for full redemption this is based on the amount in issue). The Settling Bank will then credit the South African Reserve Bank (SARB). The SARB then confirms that the funds have been received and they will advise Strate. Strate will then instruct the SARB which beneficiary banks should be credited with the proceeds based on the Record Date (RD) position.

Please note that all Capital Events (Coupon and Redemption payments) are anticipated based on the ISIN attributes at the time of Issuance. These Capital Events are all assigned a unique reference number that is common amongst the downstream systems. Thus, payment will be made per event, per ISIN and per Capital Event reference number.

Once again, this process is a proven model and is very highly automated in both the Equities and Money Market space. The benefits below have certainly been realised.

- Elimination of the risk involved with the transfer of the funds to Strate`s commercial banker.
- Faster distribution of proceeds to noteholders by eliminating the unnecessary transfer to Strate`s commercial bank account.

## Conclusion

This communication serves to specifically highlight the impacts to the Issuer community as Strate embark on a project that will bring new efficiencies to all stakeholders in the Bond market. We believe that these changes will bring vast value added improvements to the existing market across multiple stakeholders.

More detailed communications will flow going forward up until the date of implementation, which is targeted for 2nd quarter in 2017. We will begin engaging Issuers from November 2016 during one-one-one meetings and through Issuer Forums in 2017.

## Contact Details

Should you wish to find out more about these services, please e-mail [DIScommunications@strate.co.za](mailto:DIScommunications@strate.co.za), or contact **011 759 5496/5314**.

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