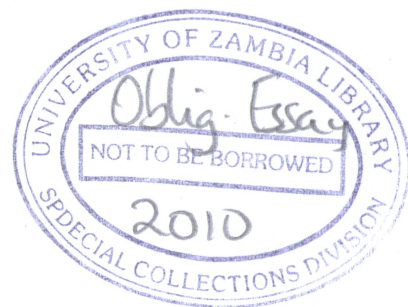


Should the Securities Act, Chapter 354 of the Laws of Zambia be amended to conform with the new developments internationally in order to be comprehensive, capture and reflect international best practice?

By

Chintu Youngson Mulendema

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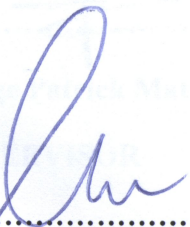
A directed research essay submitted to the School of Law of the University of Zambia in partial fulfillment of the requirement of the award of the Degree of Bachelor of Laws (LLB).

**School of Law
University of Zambia
Lusaka.**

**SCHOOL OF LAW
UNIVERSITY OF ZAMBIA
LUSAKA**

DECLARATION

I, **CHINTU YOUNGSON MULENDEMA**, do hereby declare that this research paper represents my own work, and where other people's work has been used, due acknowledgements have been made. This paper has not been submitted for any academic awards to the best of my knowledge.



.....
CHINTU YOUNGSON MULENDEMA

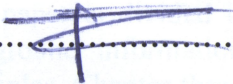
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I recommend that the directed research prepared under my supervision by Chintu Youngson Mulendema, entitled:

Should the Securities act, Chapter 354 of the Laws of Zambia be amended to conform with the new developments internationally in order to be comprehensive, capture and reflect international best practice?

Be accepted for examination. I have checked it carefully and I am satisfied that it fulfills the requirement pertaining to format laid down in the regulations governing directed research.

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Judge Patrick Matibini, (PhD), SC
SUPERVISOR

DATE 8th APRIL, 2010

ABSTRACT

Capital Markets are a barometer of a healthy economy. In Zambia, over the past two years the capital market has began to grow in terms of market capitalization and a lot of interest has been shown through purchase of portfolio investments by foreign investors, despite the worldwide financial crisis.

It is said that the share prices, unlike those of other assets, are volatile, i.e. they can either rise or fall. Therefore, they depend on the confidence the investor place on listed company's due to their conduct, and how that particular industry is performing relative to the Country's economy. Depending on the company's performance and respect for corporate governance, and its stewardship, this particular investment by investors poses significant risks because all the gains in the share price could suddenly be wiped off to zero resulting in the investors losing out all their fortunes. A case in point is the collapse of Enron in the USA and Parmalat in Italy.

Because of this uncertainty and the unbearable effect such a calamity would have on the economy and the investors, since the movement in the price of shares on the capital market is dependent on the conduct of the market players, it is imperative therefore, that the securities market is regulated effectively and efficiently in order to safeguard the interests of the investors. Internationally, an organization called the International Organization for Securities Committee, based in USA, Washington D.C, a leading international grouping of securities market regulators, was formed to specifically provide a list of international standards on the management of securities in the capital market.

Bearing this in mind and since the establishment of SEC was established over 14 years ago, it is prudent to ascertain whether the Securities Act, Chapter 354 of the Laws of Zambia should be amended to conform with new developments internationally in order to be comprehensive, capture, and reflect international best practices.

This paper is divided into four chapters. Chapter one deals with the introduction and gives background information on the research subject. Chapter two will look into the IOSCO principles, Chapter three reviews the Securities Act and chapter four consists of the conclusions and recommendations based on the findings.

ACKNOWLEDGEMENTS

First and foremost, I would like to sincerely thank my dear wife, Madryn Mumbati Mulendema, for supporting and encouraging me during my five year part time academic stint at UNZA. In her own words she always said, 'I know your plate is full to take on additional responsibilities. Currently you are managing your own Accounting Firm, CYMA Chartered Public Accountants, you are the President of the Zambia Institute of Chartered Accountants (ZICA), you serve on two other boards, traditionally you are a Senior Headman, Mulendema, and lastly, you have to look after our family' too!

Special mention goes to my Supervisor, Dr. Patrick Matibini, SC, now Judge. I would like to thank Patrick for his concise direction in my research work; especially that he only took over from the previous supervisor Mr Gabbie, who became indisposed in January 2010. This made me panic as I thought I would not complete my research paper within the approved deadline, since each Supervisor has different expectations. In his own words Patrick, 'always said that you must always differentiate consultancy work from academia'. As I dropped my pen last night, 24th of March 2010, Laura Malao phoned me that Mr. Gabbie passed on in South Africa. **May his soul rest in peace.**

I would like also to extend my heartfelt gratitude to the following: Laura Malao, Phil Kancheya, Willie Chalwe, Robert Litungu, for assisting me do this work and for being a great assistance in various ways during the course of this work.

Special thanks go to Mr. Micheal Liweleya, Captain Constance Hara and Mr. Clement Sichembe of SEC for providing me vital information and explanations for use in my work.

Finally I would like to than my classmates, who I have led as their class representative for the past five years, for showing confidence in me to lead them.

May the Good Lord Bless you all.

DEDICATION

I would like to dedicate this work to my parents Mr. David Kachingwe Mulendema and Mrs. Mary Cheepa Mulendema. My late brother and sister, Mr. Bryson Chassie Mulendema and Margaret Nyemba Mulendema, respectively. I miss your charming words of encouragement. May your soul rest in eternal peace.

My father always encouraged to give respect to every person what ever their status in society is, because these are the same people who will you choose to be their leader. He always stated “that every country passes through a river of death, so my son accept defeat and reconstruct yourself to ensure you attain your vision of assuming leadership”.

I also recall my Mother always saying to me as she escorted me to the road side and took the money from her bra, “Son, even if I give you this additional money to go to school, you will never buy me a ‘chitenge’ in my life”. True to her words she passed on without buying her clothing on 23.10.1983 at 12:00 hours, immediately I finished writing my final exams of the Zambia Diploma in Accountancy (ZDA).

My surviving brothers and sisters, Kingsley Muhumbi Mulendema, Joyce Winnie Mulendema, Daisy Mulendema, Eveness Mulendema and Chrispin Malulika Mulendema, you are the best family that anyone could possibly have. I thank God for all of you and everyday.

My special thanks go to Mrs. Jean Mulendema Katongo and Dr Katongo for organizing the Gospel singers of the Seventh Day Church to comfort me through prayers at my home for four weeks when I had a misdemeanor in January 1998.

My children, Miyoba, Abba, Cheepa. I know I have not had time for you during this period but I believe I have tried to give you the best education I can and I wish you successful careers.

God richly bless you all.

TABLE OF STATUTES

1. The Securities Act, Chapter 354 of the Laws of Zambia
2. International Organization of Securities Commission .

LIST OF ABBREVIATIONS

CIS	-	Collective Investment Schemes
IFC	-	International Finance Corporation
IMF	-	International Monetary Fund
IOSCO	-	International Organization for Securities Commission
LUSE	-	Lusaka Stock Exchange
MOU	-	Memorandum of Understanding
SEC	-	Securities and Exchange Commission
SRO	-	Self Regulatory Organization
UNDP	-	United National Development Program

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CHAPTER ONE

1.0 Background of the Study

Historically, regulation of capital markets developed in a large part, as a result of market failures-most famously following the 1929 United States of America (U.S.A) equity market crash. The massive economic disruption caused by the sudden sharp drop in equity prices, prompted governments to begin regulating issuers of securities, market intermediaries, and the of disclosure to investors, which led to improper valuation of securities, and by addressing the relationship between intermediaries, and investors. Over time, securities regulation now typically addresses a range of institutions, such as issuers, market intermediaries, investment funds and marketplaces.¹

In Zambia, this regulation is now manifested by the Securities Act ²(hereinafter referred to as ‘the Act’) upon establishment of the Securities and Exchange Commission (SEC) on 17th December, 1993.

SEC and LUSE were established with preparatory technical assistance from the International Finance Corporation (IFC), and the World Bank in 1993, as part of the World Bank and International Monetary fund (IMF) Economic Recovery Programme. The Exchange opened on 21st February 1993.

SEC is a legal persona capable of suing and being sued. The preamble of the Act states that it is an Act to:

- (i) provide for the regulation of the securities industry;
- (ii) establish the SEC and to define its objectives and functions; and
- (iii) provide for matters connected with or incidental to the foregoing.

¹ IOSCO Assessment Report 2006 pg 8

² Chapter 354 of the laws of Zambia

The securities and capital market in Zambia comprises of SEC as regulator, Lusaka Stock Exchange (LUSE), and licensed stock brokers. LUSE comprises of Stock broking firms, and is incorporated as a non-profit making limited liability company.

As indicated in the introduction, the formation of LUSE was part of the government's economic reform programme aimed at developing the financial and capital market in order to support and enhance the private sector investment initiatives. LUSE was also expected to attract foreign portfolio investment through recognition of Zambia, and the region as an emerging capital market with potentially high investment returns. Another important role of the Exchange is to facilitate the divesture of government ownership in parastatals and realization of the objectives of creating a broad and wide shareholding ownership by the citizenry, via a fair and transparent process.³

With the development of the capital market, and the world having become a one global trading market in securities, a leading international grouping of securities market regulators, called the International Organisation for Securities Committee (IOSCO), based in Washington, D.C, was set up primarily to provide best international standards on the management of securities in the capital market. The organisation's wide membership regulates more than 90% of the world's security markets. Its members regulate more than 100 jurisdictions, and its membership is steadily growing.

The preamble to IOSCO by- law states:

- securities authorities resolve to cooperate together to ensure a better regulation of the markets, on the domestic, as well as on the international level, in order to maintain just, efficient and sound markets;
- to exchange information on their respective experiences in order to promote development of domestic markets;
- to unite their efforts to establish standards, and an effective surveillance of international securities transactions;

³ ibid 5

- to provide mutual assistance to ensure the integrity of the markets by the vigorous application of the standards, and by effective enforcement against offences

It recognizes that sound domestic markets are necessary to strengthen, and develop the domestic economy and that domestic security markets are increasingly being integrated into a global market.

The IOSCO by-laws also express the intent that securities regulators, at both the domestic and international levels, should be guided by a constant concern for investor protection.⁴

The World Bank, International Monetary Fund (IMF), United National Development Program (UNDP), International Financing Corporation (IFC), do fully support the policies and imitations of IOSCO.

After fifteen years of SEC's existence it is probable that the Act may be outdated, and may not conform to international best practice as required by IOSCO. Therefore, there is need for the government to quicken the process of developing and issuing Institutional Investment Guidelines that will enable institutional investors like pension and insurance companies in Zambia, to play a more proactive role in the stock market, and make the market more liquid and attractive to investors.⁵

A market economy requires capital markets to foster economic growth by channeling savings into investment. Capital markets facilitate the ability of private enterprises, and government to issue securities and raise funds for investment and working capital needs. They provide

⁴ Objectives and principles of securities regulation OICU-IOSCO, International Organization of Securities Commissions, May 2003

⁵ *ibid* 9

secondary market liquidity necessary for capital turnover, and price discovery mechanism to ensure that capital is priced realistically and allocated efficiently⁶

Fundamental to a modern and effective securities regulatory regime is the ability of the regulator to respond in a timely, concerted and effective manner to changes in the security markets. As a result, many jurisdictions have given the authority for creating and enforcing subordinate legislation to their securities regulatory authority. This has been justified on numerous grounds, including that the legislative body lacks the time to deal with complex and detailed requirements of securities regulation. It is therefore the aim of this proposal, to determine how effective the Act is, in regulating the securities industry in Zambia, and to assess to what extent it has complied with the IOSCO standards, in order to safeguard the interests of the investors.

2.0 Statement of the Problem

The purpose of this study is to investigate the efficacy of the Securities Act with regard to the regulation of the capital market in Zambia. The Act was promulgated in 1993, and has not been reviewed or updated since then to take into account challenges in the legal and operating environment particularly issues such as the limited possibilities of trading off risk for higher returns, small size of transaction costs, high cost of information, and limited competition. It is expected that the findings of this research will inform recommendations aimed at bringing the securities regulatory regime in Zambia to the level of international best practice having due regard to the size, scope and state of development of the local securities and capital market.

⁶ International institute for securities Market Development, April 21-May 2003 Washington DC VOL 1. Policy Frameworks for Capital Market Development

There is therefore an urgent need to review and update the Act. The Act should conform to international standards because the world has become global village, in order to make trading with the outside world easier and more efficient.

3.0 Aims and Objectives

The aim of this study is investigate the effectiveness of the securities Act in regulating capital markets in Zambia

In order to assess this broad aim, the objectives are to:

- to ascertain the adequacy of the legal and institutional framework of capital markets;
- to contrast the standards prescribed in the Securities Act with those of the IOSCO;
- to identify weaknesses in the Securities Act; and
- to identify non-legal factors that impede the efficiency of a capital market;

4.0 Justification for the Study

The philosophy underlying the enactment of the Act was to provide oversight to the securities market in Zambia. This was done more than fifteen years ago and now there are more developments that have taken place which need to be included into the Securities Act in order to make it modern. During this period the way financial systems have operated, have changed significantly and markets have become more sophisticated in terms of the product range, scope of financial services, and both customers and service provider expectations. Furthermore, global financial markets have seen great upheavals which have highlighted the need for appropriate regulatory models to ensure the three principles of financial regulation, namely, investor

protection; ensuring market fairness, transparency and efficiency; and reduction of systemic risk. These include expansion of LUSE in its activities including electronic trading.

A key determinant of stock market development is the level of shareholder protection in publicly traded companies, as stipulated in securities or company laws.⁷ From the regulations that are in place, it is evident that the level of investor protection may not be adequate though the provisions of the Act provide *inter alia*, that the functions of the SEC shall be to promote and encourage high standards of investor protection and integrity among members of any securities exchange; to take considerable steps to safeguard the interest of persons who invest in securities, and to suppress illegal, dishonorable and improper practices in relation to dealings in securities, whether on the securities exchange or otherwise; and to consider and suggest proposals for the reform of the law relating to the securities industry.⁸ It is hoped that after this study, any obstacles or impediments that would be identified would be adequately addressed through the provision of answers to the questions indicated below.

5.0 Literature Review

The purpose of literature review is to read published or unpublished materials that are relevant to the topic at hand. Literature review will not only be confined to this part of the work but will continue through the whole research paper. Thus, the literature review enables one to sharpen and deepen the theoretical framework, avoid duplication of research efforts and identify the gaps in knowledge as well as weakness in previous studies.

⁷ Shleifer, Andrei and Robert Vishny 1997, A survey of Corporate Governance, *Journal of Finance* 52 (2):737-83

⁸ section 4(f) (i) (k) Cap 354 of the Laws of Zambia

Literature on the subject of regulating the securities and capital market in Zambia is scarce as the sector is still in its nascent stages and the product offering is still narrow. Therefore, the literature reviewed herein relate to the general theory on the operations of regulating capital markets especially in developed countries. Most of the researched work covers the Securities Act, unpublished reports by SEC and conference materials organised by the International Institute for Securities Market Development in Washington D.C. that have been documented and review purposes. Such unpublished works has been reviewed and provide indications on the shortcomings of the current Securities Act.

Some of the outstanding works include the following:

Gopalsamy⁹ on the need for safeguarding the interests of investors indicates that the Indian Prime Minister speaking on the occasion of the Bombay Stock Exchanges 125 years in Mumbai stressed the need to further beef up regulations and tighten surveillance mechanism of stock exchanges to provide the safest market for investors.

He discusses the need for half-yearly review of listed companies, disclosures to be made electronically, derivative products, conversion of shares into GRR'S/ADR's, insider trading, vanishing companies to mention, but a few issues.

According to the IOSCO principles, the objectives of the regulatory framework are to:

- Protect investors;
- Ensure fair, efficient and transparent markets; and

⁹ Capital Markets, the Indian Financial Scene, pg 239

- To reduce systemic risk.

The IOSCO, in its assessment report of both developed and emerging market countries argues that the increased complexity and growth of securities markets has created demand for enhanced knowledge, and understanding of the regulation of these markets and the connection between regulatory deficiencies, and other areas of the financial sector and the economy as a whole.¹⁰ It further states that the securities and derivatives markets are vital to the growth, development and strength of market economies. They support corporate initiatives, finance the exploitation of new ideas, and facilitate the management of financial risk.¹¹ Furthermore, the health of an economy increasingly relies on orderly, efficient and well regulated securities markets. Sound legal and regulatory infrastructure for securities markets is essential to protect investors.

It states that securities markets are a major component of the financial sector, and as such play a central role in the stability and development of economies. The role of securities markets which can be said to include public financing through debt, equity, and derivatives instruments-in the economy has increased globally in the past twenty years. Capitalization of equity and bond markets now dwarfs the aggregate assets of the banking systems in industrialized countries and substantially exceeds global GDP.¹²

The international lawyer¹³ expounds that some of the important areas of securities regulation are the regulation through a system of full and fair disclosure, including financial reporting based upon high quality auditing and accounting standards. It further states that effective securities

¹⁰ IOSCO assessment report of both developed and emerging market countries

¹¹ Objectives and Principles of Securities Regulation, International Organization of Securities Commissions, May 2003 pg 1

¹² According to the world federation of stock exchanges, world stock market capitalization at the end of 2000 amounted to US\$31 trillion, up from US\$17.1 trillion at the end of 1995. the market value of the bonds listed in the exchanges at the end of 2000 totaled US\$16.5 trillion, only slightly higher than the value at the end of 1995. however there are disparities between mature and emerging markets

¹³ The international Lawyer, Marc Steinberg pg 716

regulation depends upon an appropriate legal framework. The matters to be addressed in the domestic laws of a jurisdiction include an appropriate legal framework.

In this regard, the Zambia Securities Act that will be discussed in detail in chapter 2 lays a framework law that prescribes the basic institutions, organizations, principles and requirements of a system for the issue and trading of securities together with an all embracing licensing regime supported by wide supervisory and enforcement powers.

The SEC in its ongoing review of the Securities Act observes that investor confidence is cardinal for the capital market. If investors have no confidence in the market then the investor confidence will be very low and the market will stagnate.

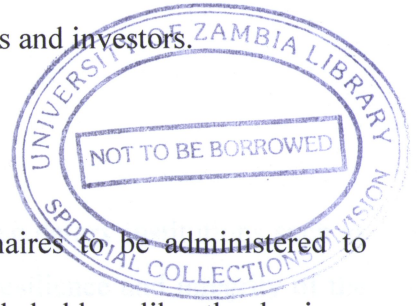
Having reviewed a number of literature as outlined above, it can safely be concluded that the Securities Act in Zambia needs to be urgently reviewed. The Act is outdated and cannot be relied upon to realize the broad aspirations of the Government and investors alike.

This proposal intends to focus on providing answers to the research question indicated above, to discern the weaknesses of the Act. The dissertation will make recommendations to redress the situation.

6.0 Research Methodology

This study will employ two methods to collect information. Namely, desk research, and field research. Desk research will cover the review of secondary sources of information, whilst field

research will include the administration of questionnaires and face-to-face interviews with various stakeholders. Namely, the management of SEC, stockbrokers and investors.



6.1 Primary Data

Primary data will be collected through interviews and questionnaires to be administered to selected stakeholders such as the SEC, LUSE, and various stakeholders like the business community and Stock Brokers. The advantages of interviews are that it enables the researcher to seek clarifications on issues and ensures that the questions are answered by the relevant person and interviews at times insure greater depth in terms of explanation. The disadvantages of interviews are that at times targeted players may not be available. On the other hand, questionnaires are inexpensive to administer and easy to plan. The disadvantages are that not all questions may be answered and some of them may be biased and not properly answered.

6.2 Secondary Data

Secondary data will be obtained from the review of modern literature as found in published and unpublished articles, books, journals, law reports, newspapers, annual reports, and workshop papers on the SEC and also on the Act. The internet will also be a significant source of literature where appropriate, and IOSCO standards. The problems that may be associated with secondary data are that some books may be out of print or outdated, articles may also not be up-date and sometimes not accurate.

CHAPTER TWO

An overview of the IOSCO principles

2.1 Introduction

One of the priorities of IOSCO is to encourage Governments and regulatory institutions such as SEC to develop and implement policies and rules that protect the resilience and integrity of the capital markets. According to SEC, IOSCO membership comprise of over 130 countries of which Zambia is a member. To support this objective, IOSCO has established 30 broad principles for implementation in the regulatory framework of every member. These principles lay the foundation as to how the capital markets should be governed by the respective securities regulator in their jurisdiction.

These principles should inform the reader a greater understanding of the operations of the capital market, and an insight into how effective and efficient the securities market is, in the discharge of its functions. This chapter assesses the IOSCO principles, and their role in ensuring that securities markets and the various players operate in an efficient and effective manner in order to protect investor's; ensure that the markets are fair, efficient and transparent and; reduce systemic risk.

2.2 Assessment of IOSCO Principles

The IOSCO principles describe a number of pre-conditions necessary for effective securities regulation¹⁴. These include, sound and sustainable macroeconomic policies conducive to investment and savings, enforceable rights, an effective legal and accounting framework, including infrastructure for clearing and settlement systems and payments), as well as corporate governance and insolvency mechanisms. IOSCO has also identified characteristics of an effective regulatory regime consistent with sound economic policies:

- There should be no unnecessary barriers to entry and exit from markets and products;

¹⁴ World Bank/IMF, Experience and Assessment of the IOSCO Objectives and Principles of Securities Regulation under the Financial Sector Assessment Program, Page 14.

- The markets should be open to the widest range of participants, who meet the specified entry criteria;
- In the development of policy, regulatory bodies should consider the impact of the requirements imposed; and
- There should be an equal regulatory burden on all who make a financial commitment or promise.

2.2.1 Principles relating to the regulator, Principles 1-5

An analysis of the principles relating to the regulator is given below:

1. The responsibilities of the regulator should be clear and objectively stated.

The above principle requires that the scope of responsibilities of a regulator is clear and objectively stated. In this regard, there should be clarity with regard to the roles of the regulator and the other agencies in the securities market such that the overall effectiveness of the regulatory regime is enhanced.

2. The regulator should be operationally independent and accountable in the exercise of its functions and its powers.

The principle of the independence of the regulator and accountability of its functions and its powers is vital for the market to operate in a fair and accountable manner. Lack of independence may result in the market operating inefficiently because of interference by authorities in the value of securities and may increase systemic risk.

The administrative control of the regulators budget by the Ministries of Finance or other government bodies is seen in some jurisdictions as having the potential to compromise operational independence.

3. **The regulator should have adequate powers, proper resources, and the capacity to perform its functions and exercise its powers.**

The above principle relates to the powers, financing and skills required by a regulator. For a regulator to effectively discharge its responsibilities, it needs adequate resources and be able to retain skilled staff. Therefore, self-financing is seen as an appropriate model to provide resources to carry out regulatory responsibilities, attract, and retain skilled staff.

4. **The regulator should adopt clear and consistent regulatory processes.**

This principle requires that the regulatory authority across several agencies should be clear and consistent. Where there is no clear demarcation of responsibility, there is lack of effective regulatory implementation, and the parties involved resort to more flexible and informal arrangements.

5. **The staff of the regulator should observe the highest professional standards, including appropriate standards of confidentiality.**

This principle places emphasis on the need for the staff employed by a regulator to possess internationally recognized professional qualifications and adhere to ethics particularly confidentiality of client interests. Continuous professional training is also key to attaining this standard. Therefore the attendance of international conferences is essential as this exposes problems experienced in other jurisdictions.

This is necessary since the engagement of poorly trained staff can lead to systemic risk.

Summary

The principles relating to the regulator emphasize the need for a regulator to possess adequate resources, independence, and scope of responsibility. These elements are necessary to ensure that capital markets are efficiently and effectively managed for the benefit of investors.

2.2.2 Principles of self-regulation, Principles 6-7

- 6. The regulatory regime should make appropriate use of the self-regulatory organizations (SRO's) that exercise some direct oversight responsibility for their respective areas of competence, to the extent appropriate to the size and complexity of the market.**

The concept of self-regulatory organizations (SRO's) is an effective way of enhancing regulation and encouraging the development of the securities industry in many jurisdictions. This is because a recognized SRO must regulate the operations and standards of practice and business conduct of its members and their representatives in accordance with its by-laws, rules, regulations, policies, procedures, interpretations and practices.

- 7. SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibility.**

According to this principle, SRO's perform delegated surveillance roles over their members. In this regard, the regulator should ensure that SRO's maintain high standards with regard to market rules and disciplinary procedures.

Summary

The principles on self regulation places emphasis on the importance of the governance and oversight arrangement structures in the SRO's. This is of utmost importance because they play a significant role in capital markets and the lack of such systems would weaken securities markets.

2.2.3 Principles for the enforcement of Securities regulation, Principles 8-10

8. The regulator should have comprehensive inspection, investigation and surveillance powers.

This principle emphasizes the need for regulators to possess adequate powers of investigation and surveillance of licensed persons. This is to ensure compliance with the law and ensure that penalties are fair and administered appropriately.

9. The regulator should have comprehensive enforcement powers.

This principle states that the regulator should enforce the law and rules by encouraging compliance through deterrence by ensuring that appropriate administrative and legal sanctions are applied in order to deter misconduct by a licensed person.

10. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.

This principle emphasizes on the need for regulator to implement systematic periodic inspections, with adequate enforcement powers that ensure that licensed persons comply with provisions of the law.

Summary

The principles for the enforcement of securities regulation emphasize the need for adequate powers of inspection, investigation and surveillance and appropriate penalties and intervention by regulators in the event of failure. This is necessary for the market to operate in an orderly manner and maintain integrity.

2.2.4 Principles for cooperation in regulation, Principles 11-13

- 11. The regulator should have authority to share both public and non-public information with domestic and foreign countries.**

This principle emphasizes the need for cross-border information sharing since the financial market has become one global village. Such information is essential for the timely identification of systemic risk and to curb money laundering activities.

- 12. Regulators should institute information sharing mechanisms that establish when and how they will share public and non –public information with their domestic and foreign counterparts.**

This principle requires that regulators put in place information sharing mechanisms such as Memorandum of Understanding (MoU). Such arrangements would facilitate cross-border investigations even though banking laws often prevent authorities from accessing such information.

- 13. The regulatory system should allow for assistance to be provided to the foreign regulators who need to make enquiries in the discharge of their functions and exercise of their powers.**

This principle requires that regulators should have provisions that allow foreign counterparts to access information required to effectively conduct enquiries also through mechanisms such as MoU's between the various regulators. The easy flow of information across borders greatly reduces systemic risk and deters fraudulent activities on the capital market.

Summary

The principles relating to cooperation between local and foreign regulators places emphasis on the sharing of information in order to enable regulators overcome legal and administrative barriers.

2.2.5 Principles relating to issuers, Principles 14-16

14. **There should be full, timely and accurate disclosure of financial results and other information that is material to the investors' decisions.**

The principle requires issuers to issue information that is detailed, timely and accurate. The information issued should meet the minimum content requirements.

Timely access to information increases the confidence of investors in the integrity of the market. The principle calls for the greater involvement by accountants and auditors.

15. **Holders of securities in a company should be treated in a fair and equitable manner.**

This principle is meant to promote equity and fairness as regards the price and value of securities amongst holders of securities (whether majority or minority) so that no party is disadvantaged and gains undue advantage through favourable treatment.

16. **Accounting and auditing should be of a high and internationally acceptable quality.**

This principle places emphasis on the need for adherence to international accounting and auditing standards as required by the International Federation of Accountants, to ensure

that there is comparability and uniformity in the information between the markets in different jurisdictions.

Summary

The principles relating to issuers are designed to ensure that the information that they disclose is accurate, timely, and meets international accounting and auditing standards. This is important because it increases the confidence of the investors and the integrity of the market.

2.2.6 Principles for collective investment schemes, Principles 17-20

- 17. The regulatory system should set standards for the licensing and the regulation of those who wish to market or operate a collective investment scheme.**

Collective Investment Schemes (CIS) are an important part of the securities markets in many jurisdictions. The principle is that there should be regulations in place to guide their operations – including the managers, the investment manager and the custodian to be licensed persons.

The lack of set standards may result in the loss of funds and result in systemic failure of investment funds.

- 18. The regulatory system should provide for rules governing the legal form and structure of the collective investment schemes and the segregation and protection of client assets**

This principle advocates for the setting up of rules regarding principals and agents with their roles being clearly defined. It also emphasizes the need for separation of the custodial responsibilities between principals and agents and also on the need to separate the assets of principals from agents.

19. **Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investors' interest in the scheme.**

This principle requires that there are comprehensive disclosure requirements regarding the evaluation of CIS's and the values thereto.

20. **Regulation should ensure that there is a proper and disclosed basis for asset valuation and pricing and the redemption of units in a collective investment scheme.**

The principle requires that there is a proper and disclosure basis for asset valuation, pricing and redemption of units in such schemes.

Summary

The principles relating to CIS's places emphasis on a strong legal requirement regime for distribution, disclosure, management and the custody of mutual fund assets. This is important because the lack of such mechanisms would reduce the governance of the CIS's.

2.2.7 Principles for market intermediaries, Principles 21-24

21. Regulation should provide minimum entry standards for market intermediaries.

The principle is concerned with the need to set minimum entry standards for market intermediaries, for example the minimum capital, prudential returns and that licensed persons are proper and fit to conduct this business.

22. There should be initial and ongoing capital and other prudential requirements for market intermediaries.

This principle emphasizes on the need for capital adequacy for market intermediaries. This is important in the event of bankruptcy/insolvency or market failure to protect investors.

23. Market intermediaries should be required to comply with standards for internal organization and operation conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.

This principle requires market intermediaries to ensure that there are adequate prudential controls in the management of risk. This is of utmost importance in order to mitigate against significant financial exposures.

- 24. There should be procedures for dealing with the failure of the market intermediary in order to minimize damage and loss to investors and to contain systemic risk.**

This principle requires the setting up of investor protection or guarantee schemes, such as Compensation Funds to mitigate losses in the event of a failure. Lack of such schemes will lead to investors incurring losses and increase systemic risk.

Summary

The principles relating to market intermediaries places emphasis on risk management and the internal organization of firms, capital adequacy, other prudential requirements and procedures in the event of failure. This is necessary because weaknesses in such areas may result in an increase in systemic risk.

2.2.8 Principles for the secondary market, Principles 25-30

- 25. The establishment of trading systems, including securities exchanges, should be subject to regulatory authorization and oversight.**

This principle requires that regulatory authorization is sought before the establishment of trading systems. This is designed to ensure that default risk and market disruptions amongst other activities are minimized. Oversight by regulators ensure maintenance of fair and equitable rules, transparency of trading, and proper management of large exposures.

28. **Regulation should be designed to detect and deter manipulation and other unfair trading practices.**

This principle is meant to ensure that clear rules are established so that the various players involved in the manipulation of market are detected immediately, and that safeguards to regulate the disclosure of price sensitive information are put in place together with appropriate sanctions.

29. **Regulation should aim to ensure that proper management of large exposures, default risk and market disruption.**

This principle emphasizes the need for the regulator to institute rules and reporting requirements which include monthly prudential returns on the financial condition of the intermediary, disclosure of funds held on behalf of other clients together with reconciliations. Analysis of major exposures by market or region and progress reports on how managements are dealing with the various risks identified and reported. The regulator on receipt of adverse market information should immediately intervene to protect investors

30. **The system for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that it is fair, effective and efficient and that it reduces systemic risk.**

This principle emphasizes the need to curb insider trading and unfair trade practices. In this regard, there should be rules and procedures to detect and deter licensed persons engaged in such activities, through periodic inspections. This would in turn ensure fairness, effective, and efficient trading and reduction in systemic risk.

Summary

The principles relating to secondary markets places emphasis on the detection of prosecution of manipulation and other unfair trading practices. This is essentially to ensure that markets operate satisfactorily, are transparent and there is adequate oversight of clearing and settlement systems. This enhances the integrity of markets and protects investor's funds.

2.4 Conclusion

This chapter has reviewed the 30 IOSCO principles with regard to the effective and efficient regulation of securities markets. As can be seen most of the provisions of the IOSCO standards are wide in scope, achieving them in full could be a challenge for a regulator such as SEC. Compliance with the IOSCO standards would enhance investor protection; ensure that the markets are efficient and transparent; and reduce systemic risk. The next chapter deals with the reviews of the Securities Act with relation to its compliance or non compliance with IOSCO principles and standards.

CHAPTER THREE

Review of the Securities Act

3.1 Introduction

The Securities Act prescribes the basic institutions, organizations, principles and requirements of a system for the issue and trading of securities, together with an all-embracing licensing regime supported by wide supervisory, and enforcement powers. In addition, the Securities Act also contains numerous provisions providing for passage of subsidiary legislation by the Commission, to provide the detail of the securities regulation.

This chapter reviews the Securities Act that was enacted in 1993. It assesses the institutional framework prescribed by the Securities Act, and analyses how it is functioning vis-à-vis the international best practices as set out by the IOSCO. As indicated in the introduction, securities markets world over have witnessed the occurrence of scandals induced by manipulation, and insider trading such as Enron and Parmalat in the USA and Italy respectively. Therefore, in order to pre-empt the occurrence of similar events in Zambian capital market, there is urgent need to review, and strengthen the Securities Act and conform it to international best practices as espoused by IOSCO.

3.2 Institutional framework

According to international best practices, the institutional framework of securities market comprises six layers of institutions. These are compliance offices at firm level, stock exchanges as Self Regulatory Organizations (SRO), the Securities and Exchange Commission as regulators, the Government with the authority to give direction on policy issues after consultations with stakeholders, and the High Court and Supreme Courts to hear cases on appeal.

The Securities Act provides for the establishment of SEC as the highest executive body. It has supervisory authority of the securities market in the country. It is an autonomous administrative body reporting to the Minister of Finance.

SEC is responsible for making basic decisions, including approval of the Exchange's Rules and Regulations, as well as operating conditions through various committees. Namely, Registration, Finance and General Purposes, Mergers and Takeovers, Licensing, Publications and Compensation Fund. SEC is additionally responsible for appointing and supervising general management. It also approves the trading and settlement systems.

The above structures conform to international IOSCO standards, and the market is divided into primary and secondary markets. SEC is also not a self financing body and is funded by the national treasury due to the fact that capital market is in its nascent stage. It however collects commission both from the sell and purchase of shares at LUSE.

The aim of Government is to make it self-sustaining in future. LUSE has a membership of 21 listed companies, namely, African Explosives Limited Zambia, Bata, British American Tobacco Zambia, BP Zambia, Cavmont Capital Holdings Zambia, Copperbelt Energy Company, Zain Zambia, Larfarge, Farmers House, Investrust, NATBREW, Pamodzi, Standard Chartered Zambia, Shoprite, Zambeef, ZAMEFA, ZAMBREW, ZCCM-IH, ZANACO and Zambia Sugar.

According to the Stockbrokers Zambia Limited, LUSE had a market capitalization of Kwacha 25.4 billion as at 5 March 2010.

3.2.1 Governance

The Securities Act provides under Part 2, that the Commission exists as a statutory body with perpetual succession; a common seal; capable of suing; and being sued; and subject to the provisions [of the Act], capable of performing all such acts as a body corporate may by law do or perform.

The Commission comprises of not more than seven, nor less than five individuals who shall be appointed by the Minister as follows:

(1) Five of the members of the Commission shall be nominated by the following organizations, with each organization nominating one individual for appointment by the Minister;

- (a) the Bank of Zambia;
- (b) the Law Association of Zambia;
- (c) the Zambia Institute of Chartered Accountants;
- (d) the Zambia Chambers of Commerce and Industry; and
- (e) the Ministry of Legal Affairs.

(2) Two of the members of the Commission shall be selected from among those persons who appear to the Minister to have wide experience and ability in legal, financial, business, investment or administrative matters to become Chairman and Vice Chairman.

3.3 Overview to securities regulation

Securities regulations play a critical role in fostering the development of the entire economy. They also play an equalizing role by enabling wider participation by a greater number of people who share in investment opportunities, as well as business and market risks.

A sound legal and regulatory framework for securities is essential to protect investors. It is therefore of critical importance that the regulations governing the operation of capital markets promote a system of full and fair disclosure, have water tight customer protection rules, capital adequacy standards, market transparency, clearance and settlement safeguards, market surveillance, and avoidance of barriers to fair competition.

Other pertinent matters relate to regulatory compliance, including brokerage firm, stock exchange and investment company inspection procedures; and enforcement programmes, designed to protect investors and preserve the integrity of the securities markets, that provides for adequate investigatory authority, and remedies with respect to insider trading, market manipulation and financial fraud.¹⁵

¹⁵ United States Securities and Exchange Commission Report

In this regard, the imposition and effective enforcement of rules, which ensure the market is operated efficiently, is of utmost importance.

3.4 Review of the Securities Act

The Securities Act is arranged into eleven sections and each section will be reviewed. The sections consist of part one, **Preliminary**; part two, **Securities and Exchange Commission**; part three, **Securities Exchange**; part four, **Licensing of dealers**; part five, **Registration of Securities**; part six, **Conduct of Securities Business**; part seven, **Improper Trading Practices**; part eight, **Powers of intervention**; part nine, **Compensation Fund**; part ten, **Collective Investment Scheme and part eleven, Miscellaneous**.

3.4.1 Preliminary

Like most Acts of parliament, the preliminary section of the Securities Act provides the short title and the interpretation. The terms included under definitions and interpretations include ‘dealing’, securities’ and ‘exchange rules’. Other definitions that are provided for in the Act are words like underwriter, share, securities market, registered securities to mention but a few.

For example, the term ‘dealing’ would have a different interpretation if read by a layperson. According to the Act, dealing is defined, in relation to securities dealing meaning acquiring, depositing of, subscribing for or underwriting securities or making or offering to make with any person, or inducing or attempting to induce a person to enter into or offer to enter into, an agreement relating to the acquisition or disposal of, subscription for or underwriting of securities.

The definition of a company and a subsidiary are not similar to those that are provided for in the company’s Act of 1994. Further, the Act should have provisions that enable for the enactment of subsidiary legislation by SEC. Some definitions in the Act need to be updated and also new terms need to be added such as Central Securities Depositories (CSD), Subsidiary, Immobilize, Prospectus, and Securities Exchange as defined below.

‘Central Depository’ or ‘CSD’ should mean a company licensed as a central depository or should mean a company.

‘Subsidiary company’ is not defined. The term should have the meaning as under Section 43(3) of the Companies Act Chapter 388 of the laws of Zambia.

‘Immobilize’ should mean to deposit, with a central depository or agent physical holdings or scrip in exchange for a book entry on the electronic records of the central depository.

‘Prospectus’ should mean any prospectus, notice, circular, brochure, advertisement, publication, or other document – offering to the public for subscription or purchase any securities or calculated to invite offers by the public to subscribe for or purchase any securities.

‘Securities Exchange’ should mean exchange established by a company licensed to do so.

Further the definition of “exchange rules” is given and this means in relation to the securities market that the rules made by the exchange that are binding on its members or any of them.¹⁶

3.4.2 Securities and Exchange Commission

The second part of the Securities Act provides for the existence of SEC as a statutory body with perpetual succession as indicated in section 2.2.1 above. The main purpose of the body is to regulate securities, the securities markets, the intermediaries that operate in those markets, the issuers of securities, and the sale of interest in, and the management and operation of, collective investment schemes. In summary, the objectives of regulatory framework are to protect: (a) investors; (b) to ensure fair, efficient and transparent markets; and (c) to reduce systemic risk.

A review of the Act shows that the Securities Act presently accords LUSE membership of the SEC board. Currently the members of the commission include a representative from LUSE an organization regulated by SEC. This is in conflict with the principles of corporate governance.

¹⁶ interpretation section securities Act

According to IOSCO standards, it is not appropriate for a representative of an entity that is regulated by the Commission to serve on the governing body.

One key issue that is not addressed is a provision providing for the securities tribunal to adjudicate on the administrative decisions made by the Commission.

SEC is not operationally independent from the Ministry of Finance (MoF) especially that it is not self financing and the members of the Commission are appointed by the Minister. This contrasts significantly from The Romanian National Security commission which is self financing and raises fees from its constituencies.

3.4.3 Securities Exchanges

Part III of the Securities Act relates to the activities of Securities Exchanges. The main purpose of this section is to establish securities exchanges in other parts of the country as what obtains in other jurisdictions. It further sets out the rules of how a person can establish a securities exchange and how one should hold himself as providing, or maintaining a securities market.

The part has provisions relating to the establishment and maintenance of a securities exchange and the penalties for non-compliance. The part also describes the relationships between the SEC and the Securities Exchange.

Other provisions include rules for amendments to existing exchange regulations and penalties for operating unlawful securities market. The act specifically mentions LUSE as having been deemed to have been created under the Act.

Section 9(3) deals exclusively and specifically with the LUSE, meaning that no other stock exchange would be set up within Zambia. This part should be deleted to ensure that additional securities exchanges may be established in the future.

3.4.4 Licensing of dealers, Investment Adviser and Representatives

Part IV of the Act contains provisions relating to the licensing of dealers, investment advisers and representatives by SEC. This is the section contains the rules and procedures of how the dealers, underwriters, investment advisors are to be licensed. It also defines the qualification of these intermediaries and the how a license can be revoked.

Section 26 (1) states that any person aggrieved by a decision of the Commission, may within thirty days of the date of the decision appeal to the court. The decision of the Commission is not stayed by the lodgment of an appeal.

This process is cumbersome and there is no securities tribunal to hear and determine appeals on the administrative decisions made by the Commission.

3.4.5 Registration of Securities

Part V of the Act relates to the registration of securities. In order to protect the investors whenever a security becomes publicly traded, directly or indirectly traded or advertised or offered for sale to the public it should attract the obligation to file a registration statement, referred to as a prospectus.

Under the Act, it is a requirement that all securities are registered with SEC. It is a requirement that the prospectus that is prepared for public offers contains all such information as investors and their professional advisers require for the purpose of making any decision or informed assessment of the assets and liabilities, financial position and losses and the prospectus of the issuer of the securities and rights attaching to the securities.

A notable weakness under the Securities Act is that there is no requirement for disclosure and notification of substantial interests in the securities of the company's listed and interests of connected persons to give notice of changes in such companies.

There is no provision relating to civil liability, and the rights of investors for mis-statements or omissions in the prospectus. This should be amended to conform to section 129 of the Companies Act, Chapter 388.

3.4.6 Conduct of Securities Business

Part VI of the Act refers to how the securities business is to be conducted and the penalties for non-compliance. The main purpose of this section is to protect investors from being exposed to the risk of loss where there is no security given in a case where the principal has not given any collateral to the agent.

It prescribes a code of conduct with respect to conduct in the securities business. It prohibits short selling and contains rules for or in respect to the segregation of client moneys or other property and for the conduct thereof by investment advisers. It also defines how a takeover or substantial acquisition of securities of any company should be conducted.

However, a weakness noted under this section, is that there is no provision where a person who is selling as agent requires the principal to place 100% collateral against the short sell marked to market at the cost of every trading day until the transaction is completed.

3.4.7 Improper Trading Practices

This part of the Act refers to improper practices in the securities market. The main purpose of this section is to deter dishonest conduct by persons whose ulterior motive is to gain through willful manipulation of information regarding the performance of the company's shares, when in fact the said shares are not performing as published. It also prohibits directors and employees and connected persons from disclosing price sensitive information of the listed companies to the public.

It refers to amongst other issues to false trading and manipulation of the market, the use of deceptive statements, fraudulent transactions, false or misleading statements in connection with

the sale of securities, insider trading, the powers of inspection and also damages for loss sustained through contravention of the provisions of this part of the Act which covers areas relating to improper trading.

The section covers in detail the various prohibitions and types of offences ranging from creation of false or misleading appearance of the volume of trading, maintaining or inflating, depressing or causing fluctuations in the market price, use of deceptive statements as a means of inducing another person to deal in securities either by the making or publishing any statements, promise or forecast that he knows to be misleading, false or deceptive, by dishonest concealment of facts.

Insider dealing is not allowed by any person who counsels or procures another person to deal in securities of a company concerning which he has any knowledge that is not publicly available, materially affecting the price of the securities.

Section 52(1) is the only section dealing with insider trading. It is my considered view that there should be a separate and more detailed Part for Insider Trading. Secondly, the penalties under the current Act state that a person if found guilty, shall be liable on conviction to a fine not exceeding two hundred thousand penalty units or to imprisonment for a term not exceeding five years or to both. This penalty gives the Courts the discretion to either make the offender pay a fine or be imprisoned. The capital market has become very sophisticated in regard to new products; scope of financial services therefore there is need to enhance the provisions relating to penalties on insider dealing.

There are no specific powers to cooperate with and provide assistance to overseas regulators.

3.4.8 Powers of Inspection

The purpose of this section is to give powers to the Commission to carry out inspections and investigations on listed companies, dealers, stock brokers and investment advisers and obtain assurance that the information that they submit to SEC is of integrity. SEC should also have the power to enter premises of a licensed person and obtain information as required by this Act. For example section 53 (1) states that the Commission may from time to time inspect under

conditions of secrecy the bank accounts, documents and transactions of a person licensed under this Part.

The section on inspection is inadequate and should be expanded to allow the Commission to enter premises of the licensed person, to make enquiries of a licensed or any other person it believes has information relating to any record or document concerning any transaction being investigated.

Further, there is need to harmonize the Securities Act with the client confidentiality provisions of the Banking and Financial Services Act such as access to bank accounts.

3.4.9 Powers of Intervention

Part VIII of the Act relates to the powers of intervention. The main purpose of this section is to carry out investigations on complaints received or where the Commission has reasonable cause to believe that an offence has been committed by a licensed dealer who is engaged in fraudulent activities or misconduct in regard to registered securities.

In this regard, a person will have committed an offence if he has furnished the Commission with information that is false, inaccurate or misleading. The Commission has powers to prohibit a licensed person from entering into transactions of a class or description specified in the notice, soliciting business from persons of a class or description so specified, or carrying on business in a specified manner. It also has powers to restrict on dealing with assets whether in Zambia or elsewhere to prohibit a person so licensed from disposing of such assets. Further it has powers to require a person licensed under this act to maintain in Zambia assets of such value as appears to the Commission to be desirable, with a view to ensuring that the licensed person will be able to meet his liabilities with respect to which the business relates. The Commission may, either on its own motion or on the application person licensed on whom a prohibition or requirement has been imposed, rescind or vary the prohibition if it appears to the Commission that its is no longer for the prohibition or requirement to take effect or to continue.

Section 271(1) of the Companies Act, Chapter 388 does not recognize SEC as an institution that can present a petition under the companies Act and there is no provision relating to the distribution of the assets of a person on insolvency, bankruptcy or winding up on the appointment of a receiver over any assets of a person.

3.4.9 Compensation Fund

Part IX of the securities Act relates to the Compensation Fund. The purpose of the compensation fund is that of compensating persons who suffer pecuniary loss occasioned by any default of a licensed dealer or licensed investment advisor. The minister shall establish and maintain a compensation fund.¹⁷ The Act also provides that there shall be a compensation fund committee which shall be responsible for the administration of the compensation fund; the committee shall compose of nominated members from some sectors that are provided for in the Act.¹⁸ The members of the committee shall elect one member amongst themselves to be the chairman of the committee.¹⁹ The purpose of the fund is to compensate innocent parties who suffer lose as a result of the dealers or investment advisors.²⁰ Provisions relating to the disbursement of funds are found in section sixty-eight of the Act. The minister may make regulations prescribing all such matters and tings as are necessary or expedient to be prescribed for or with respect to the administration, management and application of any compensation fund established under the Act.²¹ Payment from the fund shall be limited, in respect of each license in default, to such amount as the minister may by regulation provide.²² Any disbursement from the compensation fund that is accountable to the default of any licensed person is a debt due to the fund and is recoverable at the suit of the commission in any court of competent jurisdiction²³ and as per the definition of court it is provided for in the definition section as being the High Court of Zambia.

The provisions of this section are adequate and safeguard the interests of investors.

¹⁷ section 64

¹⁸ section 65(2)-(e)

¹⁹ section 65(3)

²⁰ section 67

²¹ section 69

²² section 70

²³ section 71

3.4.10 Collective Investment Scheme

Part X relates to Collective Investment Scheme (CIS). According to the definition that is provided for in the Act, "collective investment scheme" means any arrangements with respect to money or other property of any description, under which-

(a) provision is made for persons taking part in the arrangements to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income;

(b) property the subject of the arrangements-

(i) is owned or held in trust by; or

(ii) is managed by or on behalf of,

a body corporate (in this Part referred to as the "operator" of the scheme); and

(c) the interests of persons participating in the arrangements is represented by shares or other securities of the body corporate or, in the case of a unit trust, by units;

(d) funds invested in accordance with the arrangements purporting to be invested with the aim of spreading investment risk.

"investment company" means a company that is the owner of property the subject of a collective investment scheme;

"open - ended investment company" means an investment company whose collective investment scheme makes provision for-

(a) redemption or repurchase, by (or out of funds provided by) the company, of shares, securities or units representing the interests of participants in the scheme; or

(b) the sale of such shares, securities or units by the participants on a securities exchange at a price related to the value of the property the subject of the scheme;

"unit trust" means a collective investment scheme in which:

(a) property the subject of which the scheme is held on trust for the participants of the scheme by a person other than the operator of the scheme; and

(b) the interests of participants in the scheme is represented by what are commonly known as units in the trust or by a mode of representation, by whatever name described, that the Commission considers equivalent.

The commission may authorize collective investment schemes for the purpose of this part of the Act.²⁴ Any such authorization by the commission may be granted subject to such terms and conditions as the commission considers being necessary and desirable for the protection of investors.

The current Act does not recognize an overseas collective investment scheme and no person may publicly promote a Collective Investment Scheme in Zambia unless it has been authorized by the Commission²⁵.

3.4.11 Miscellaneous

Under Part XI of the Act contains miscellaneous provisions. The provisions under this section relates to any other matters that have not been addressed by the Parts above. It covers issues regarding furtherance of its regulatory objectives and any matters relating to the functions of the Commission. It provides for immunity of the Commission where in the performance any power, authority, duty where it is shown that the omission has been done in good faith. It also provides for offences by bodies corporate. The Commission has also a mandate to make rules by way of a

²⁴ section 73

²⁵ Interview with Michael Liweleya, Director, Operations and Licensing at SEC

statutory instrument with respect to any matter that the Act is permitted or required to be prescribed.

3.6 Conclusion

Securities regulations as discussed above enable all participants in the market to have the confidence in its integrity. The integrity of the market is supported by rules, which impose capital requirements, through the provision of investor insurance and by ensuring that there is a process available for resolution when the market appears to be abused by participants.

The review of the Securities Act indicates that it is outdated, and the institutional framework needs urgent review to cater for the establishment of tribunals, provide for a separate insider trading Part, the commission must be given additional powers of inspection and to cooperate with and provide assistance to, overseas regulators to mention a few.

CHAPTER FOUR

Conclusions and Recommendations

This chapter comprises the conclusions and recommendations of the research.

Conclusions

The analysis of the Securities Act in the foregoing chapters demonstrates that the Act partially conforms to the IOSCO principles, and there does not effectively regulate the securities market in Zambia.

Amongst the key weaknesses identified in the analyses include the following:

- 1) Some of the definitions and terms and in the preliminary section such as ‘Central Securities Depositories’, ‘subsidiary company’, ‘immobilize’, ‘prospectus’, ‘securities exchange’, ‘Clearing Agency’ are narrow or omitted.
- 2) Currently, under the Act, it is the Minister who has the power to pass subsidiary legislation. This brings about bureaucracy and red tape in the passing of rules and regulations.
- 3) The Commission does not have adequate supervisory and investigative powers; and express powers to enter the premises of the licensed person, to make enquiries of the licensed or any other person it believes has information relating to any record or document concerning any transaction being investigated.
- 4) LUSE is regulated by SEC; however, it is a current requirement that it nominates a representative for appointment as Commissioner. This creates a conflict of interest as LUSE is regulated by it.

- 5) The Securities Act has no explicit provisions for SEC to co-operate with foreign regulators or authorities independently to follow up on illicit activities of foreign investors.
- 6) In the Securities Act there is no requirement for disclosure and notification of substantial interest in the securities of the companies listed, and interest of connected persons to give notice of changes in such companies.
- 7) The current Act does not recognize an overseas Collective Investment Scheme.
- 8) There is no provision for a person who is selling as agent requiring a principal to deposit 100% collateral against the short sell marked to market at the cost of every trading day, until the transaction is completed.
- 9) There is only one section dealing with insider trading. This is insufficient.
- 10) SEC's is undercapitalized and therefore it has been unable to effectively carry out its functions viz. education of investors about the benefits and risks of trading in shares and enforcing the rules and regulations.
- 11) There are inherent conflicts in the laws and regulations that govern the securities market. There are conflicts between the Companies Act, the Securities Act and the Banking Laws. For example the Banking Financial Services Act requires that consent must be obtained from the customer to access their bank account. Whereas SEC has powers to inspect statements of those customers who have accounts with a particular Bank, dealing in the securities market.

Secondly, it is also a requirement that all banks publish their prudential performance on a quarterly basis, including those listed on LUSE. This works against the principle of insider trading as the results of the listed banks are published before they are audited and therefore are likely to affect the share prices.

Thirdly, SEC under the Company's Act is not recognized as an institution that can present a petition for winding up of licensed entities. Further, there is no provision relating to the distribution of the assets of a person on insolvency, bankruptcy or winding up, on the appointment of a receiver over the assets of a person.

- 12) There is no provision relating to civil liability, nor are the rights of investors provided for in the Act for misstatements or omission in the prospectus as is defined in the Companies Act.

In view of the foregoing, it is clear that the Act is outdated and requires to be repealed immediately in order to effectively safeguard the interest of investors.

Recommendations

In light of the above conclusions, it is recommended that the following matters be incorporated in the proposed new legislation in order to conform with the IOSCO principles and modern practices.

- 1) The definitions must be expanded and new terms should be included.
- 2) The power to pass subsidiary legislation should be delegated to SEC to bring about efficiency in its operations.
- 3) SEC should have adequate supervisory and investigative powers; and express powers to enter the premises of the licensed person, to make enquiries of the licensed or any other person it believes has information relating to any record or document concerning any transaction being investigated.
- 4) LUSE should not be allowed to nominate a representative for appointment as a Commissioner of SEC.

- 5) The Securities Act should have explicit provisions for SEC to co-operate with foreign regulators or authorities independently to follow up on illicit activities of foreign investors.
- 6) The Securities Act should have requirements for disclosure and notification of substantial interest in the securities of the companies listed, and interest of connected to give notice of changes in such companies.
- 7) The proposed new legislation should recognize an overseas Collective Investment Scheme in order to encourage participation of foreign investors in the local securities market.
- 8) There should be a provision in the new legislation for a person who is selling as agent requiring a principal to deposit 100% collateral against the short sell marked to the prevailing market price of every trading day until the transaction is completed.
- 9) The section dealing with insider trading should be expanded into a separate part in the new legislation. The rules and regulations should be expanded; the Courts should not have discretionary powers to either charge a penalty or imprisonment.
- 10) SEC's should be fully capitalized for it to effectively carry out its functions viz. educating of investors about the benefits and risks of trading in shares and enforcing the rules and regulations.
- 11) The inherent conflicts in the laws and regulations that govern the securities market between the Companies Act, the Securities Act and the Banking Laws should be harmonized to render an efficient and effective regulatory financial system.

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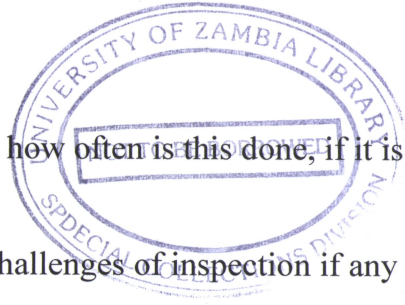
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APPENDIX

QUESTIONNAIRE

1. Are the laws, regulations, procedures and contractual provisions governing the securities settlement arrangements public and readily accessible to system participants?
2. Does the legal framework demonstrate a high degree of legal assurance that
 - (a) Transactions are enforceable
 - (b) Customers assets are adequately protected (particularly against the insolvency of custodians and intermediaries)
3. Are the rules of the system and contracts between system participants enforceable notwithstanding the insolvency of a principal?
 - (b) Is there a significant level of cross border participation in the securities settlement system?
 - (c) Are other jurisdictions relevant for determining the adequacy of the legal framework? If so how is it determined?
4. Has the legal framework been evaluated in comparison with other relevant jurisdictions?
5. Are there any conflict of law issues and so, have they been addressed?
6. Are investor laws in Zambia strong enough to encourage investors to invest on the Zambia security market and if not, what in your view should be done to enhance investor protection?
7. Is there market fairness, transparency and efficiency; if not what suggestions do you have that will help foster the development of these aspects?
8. What is the level of systemic risk in Zambia and how can it be reduced?
9. How does the SEC ensure compliance of the SEC rules and regulations by all stakeholders, including
 - Market participants
 - Broker participants
 - Broker dealers
 - Investment advisers
 - Investment companies
 - The stock exchange



Section 4 (e) (c) provide for periodic inspection how often is this done, if it is done?

10. How does the security exchange deal with the challenges of inspection if any are faced?
11. Is disclosure in the securities laws considered as one of the most important components?
12. Do you think that the laws on insider trading are adequate particularly looking at section 52 (3) doesn't this provision disqualify the whole provision or is it intended to protect the party?
13. Does taking action against securities fraud and monitoring for illegal transactions, securities regulators complement the work of law enforcement authorities charged with combating money laundering and similar financial crimes?
14. Does Zambian security market face any challenges related to money laundering? Have any detection been made or is it that the detection mechanisms in place are not up to date?
15. What controls in your view can be put in place to help limit possible customer losses?
16. Does the SEC produce any brochures to educate the public and if so how often does this happen?
17. In your view are the Zambian citizens enlightened about the security market?
18. The definition of court is high court; does this mean that the only court recognised by the SEC is the high court? (Definition section)
19. Looking at Section 10(2) how can the securities exchange go to prison, isn't it the officials who work there who are supposed to be imprisoned?
20. What measures does the SEC take to ensure that unlicensed dealers do not deal in securities?
21. Section 53 refers to secrecy – does this mean without the knowledge or a person who is licensed to deal in securities or does it refer to not publicizing that an investigation is being undertaken?
22. How do you ensure liquidity of the market