

Liability of intermediaries for shortfall and unauthorised disposal. The Nigerian context.

Segun Sanni.

Head, Investor Services

Stanbic IBTC Bank Plc

Lagos, Nigeria.

A member of the Standard Bank Group of South Africa.

E-mail: segun.sanni@stanbicibtc.com

Paper delivered at the UNIDROIT colloquium on promoting investor confidence and enhancing legal certainty for securities trading in emerging markets.
Venue: Windsor Atlantica Hotel, Cobacabana, Rio De Janeiro, Brazil.

Date: 27th March 2012.

Shortfalls and unauthorised disposal in the context of UNIDROIT

- The main purpose of the UNIDROIT convention is to offer harmonised transactional rules to reduce the legal risks associated with intermediated securities especially across borders.

The Nigerian position on intermediated securities.

- Unlike the U.S and other advanced markets, the system of laws governing intermediated securities is still evolving in Nigeria.
- Our basic framework for the owning, holding and transfer of securities is, in some respects, obsolete, and fragmented.
- We have CAMA, ISA, BOFIA and SEC Rules. A few of the provisions seem contradictory, some ambiguous.

The Nigerian position (cont'd)

To attract significant international flows, the limitations would need to be addressed.

Nigeria will benefit immensely from the UNIDROIT initiative to leapfrog our governing rules and regulations to meet international standards and the complexities of today's financial markets.

The current regulations on shortfalls and unauthorised disposal

- The applicable regulations are covered in the ISA 2007 and SEC Rules.

SEC Rule No 27 (regulation of custodians)

- 5b. A custodian of securities shall have appropriate safekeeping measures to ensure that such securities are protected from theft and other hazards.
- 12. A custodian of securities is prohibited from disclaiming responsibility for losses of investments due to fraud, willful default or negligence arising from its acts or omission or those of its agents appointed by it in the course of performing its custodial services.

SEC Rule No 27 (regulation of custodians) (cont'd)

- 13. A custodian of securities shall be responsible for irreconcilable shortfalls in the quantity of investments identified on a reconciliation of client's investments.
- 14. The custodian must ensure that it (or its nominee) acts only in accordance with:
 - a. Client's instructions
 - c. It accepts responsibility in writing to its clients for any of the nominees used, to the same extent as for its own actions.

SEC Rule No 27 (regulation of custodians) (cont'd)

- 15. A custodian or sub custodian shall ensure that:
- b. it, or its appointed sub custodian, acts only on instructions given in accordance with the agreed procedures.

SEC Rule No 27 (regulation of custodians) (cont'd)

- Code of conduct for custodians of securities.
- 1. Maintain the highest standard of integrity, fairness and professionalism in the discharge of its duties.
- 3. Be continuously accountable for the movement of securities in and out of the custody account, deposit and withdrawal of cash from the client's account and shall provide complete audit trail, whenever called for by the client or the Commission.
- 4. Establish and maintain adequate infrastructural facilities to be able to discharge custodial services to the satisfaction of clients, and the operating procedures and systems of the custodian of securities shall be well documented and backed by operations manuals.

SEC Rule No 27 (regulation of custodians) (cont'd)

- 9. Exercise due care and diligence in safekeeping and administration of the assets of clients in its custody for which it is acting as custodian.

Other safeguards for the owner of securities.

- Similar rules exist for other market participants.
- SEC rules on adequate capitalisation.
- Investor Protection Fund (IPF).
- Custody agreements and due diligence in appointment of custodian

Some pertinent questions

- What constitutes a shortfall?
 - Can an unpaid corporate action constitute a shortfall?
 - Can a possible nationalization be construed as a shortfall?
- Can a claim of unauthorized disposal be made only by the account owner and not by a previous holder?
 - Live case in Nigeria where a party wilfully transferred securities to a party but later sued the party's custodian when party sold securities.

Conclusion

- From the foregoing, there are rules in place to protect investors against shortfalls and unauthorised disposals in Nigeria.
- Though there may be disputes among parties, a well defined system of laws/rules will facilitate adjudication on such disputes.
- Harmonisation with UNIDROIT convention would help remove all limitations and ambiguities and assure investors on the mitigation of the legal risks in their assets held in Nigeria.

Thank You.

Questions.