

LAWS OF KENYA

**THE CENTRAL DEPOSITORIES (AMENDMENT)
ACT**

No. 38 OF 2011

Published by the National Council for Law Reporting
with the Authority of the Attorney-General

THE CENTRAL DEPOSITORIES (AMENDMENT) ACT

No. 38 of 2011

Date of Assent: 2nd December, 2011

Date of Commencement: 16th December, 2011

AN ACT of Parliament to amend the Central Depositories Act, 2000 and for connected purposes

ENACTED by the Parliament of Kenya as follows-

Short title.

1. This Act may be cited as the Central Depositories (Amendment) Act, 2011.

Amendment of section 2 of Act No. 4 of 2000.

2. The Central Depositories Act, 2000, in this Act referred to as the "principal Act", is amended in section 2-

(a) by deleting the definition of "central depository" and substituting therefor the following new definition-

"central depository" means a company licensed by the Authority to —

(a) establish and operate a system for the central handling of securities —

(i) where securities are deposited and held in custody by, or registered in the name of, the company or its nominee company for depositors and dealings in respect of these securities are effected by means of entries in securities accounts without the physical delivery of certificates: or

(ii) which permits or facilitates the settlement or registration of securities transactions or dealings in securities without the physical delivery of certificates; and

(b) provides other facilities and services incidental thereto;

(b) by deleting the definition of "central depository agent" and substituting therefor the following new definition-

"central depository agent" means a person appointed as an agent of a central depository to carry out one or more of the services provided by that central depository;

- (c) by deleting the definition of "securities exchange" and substituting therefor the following new definition-

"securities exchange" means a market, exchange, securities organization or other place at which securities are offered for sale, purchase or exchange, including any clearing, settlement or transfer services connected therewith;

- (d) by deleting paragraph (c) in the definition of securities and substituting therefor the following paragraph —

- (c) derivatives including futures and options contracts on securities, indices, interest or other rates, currency, futures or commodities.

- (e) by deleting the word "stock" appearing in the definition of "stock market and substituting therefor the word "securities";

- (f) by inserting the following new definitions in proper alphabetical sequence —

"default process" means actions taken by a central depository under the default rules;

"default rules", means rules of a central depository that provide for the taking of action by a central depository, against a defaulter;

"defaulter" means a central depository agent who is subject to any default process;

"market charge" means a fixed or a floating charge, granted by a central depository agent to a central depository over any property which is held by or deposited with the central depository for securing liabilities, arising directly in connection with the central depository, for the settlement of a market contract;

"market collateral" means any property which is held by or deposited with a central depository for the purposes of securing liabilities, arising directly in connection with the central depository, for the settlement of a market contract;

"rules" means rules, by-laws or such other instruments made by a central depository or contained in its constituent documents, which govern the activities and conduct of a central depository and its agents and other persons in relation to it; and

"substantial shareholder" means a person who has a beneficial

interest to or exercises the voting rights attaching to such percentage of the issued share capital of a central depository as may be prescribed by the Authority from time to time.

Insertion of section into Act No. 4 of 2000.

3. The principal Act is amended in Part 11, by inserting the following new section immediately before section 3 -

Functions of the Authority.

2A. The functions of the Authority under this Act shall be to-

- (a) take such measures as are necessary to ensure that the provisions of this Act are complied with;
- (b) take necessary measures to maintain and promote fairness, efficiency, competitiveness, transparency and orderliness in the deposit of securities, and the clearance and settlement of transactions in securities, by a central depository;
- (c) licence, supervise, monitor and regulate the activities of central depositories;
- (d) set standards of competence for central depository agents;
- (e) approve the rules of central depositories;
- (f) promote, encourage and enforce proper conduct, competence and integrity of central depository agents;
- (g) counter and suppress illegal, improper or unfair practices;
- (h) make regulations for the better carrying out of the purposes and provisions of this Act; and
- (i) perform any other functions under this Act or any other legislation as may be conferred, from time to time, on the Authority.

Repeal and replacement of section 4 of Act No. 4 of 2000.

4. The principal Act is amended by repealing section 4 and replacing it with the following new section-

Establishment of a central depository. Cap. 486.

4. (1) A company incorporated under the Companies Act which

proposes to operate a central depository shall apply to the Authority in writing to be licensed as such.

(2) An application under subsection (1) shall be accompanied by-

(a) the CDS Rules made by the applicant in such manner and form as the Authority may prescribe;

(b) the prescribed fee; and

(c) such other information as the Authority may prescribe.

(3) The Authority may require an applicant to provide such further information as it may consider necessary in relation to the application, in such form or verified in such manner as the Authority may direct.

(4) A central depository which proposes to alter any particulars submitted under this section shall seek prior approval of the Authority before making such alterations.

(5) The Authority shall, in considering an application under subsection (1), determine if the applicant is fit and proper for the purposes of this Act.

Insertion of section into Act No.4 of 2000.

5. The principal Act is amended by inserting the following new section immediately after section 4 —

Determination of fit and proper.

4A. (1) The Authority shall, in determining whether a person is fit and proper under section 4(5), consider the-

(a) financial status or solvency of that person;

(b) educational or other qualifications or experience of the person, having regard to the nature of the functions which, if the application is granted, the person shall perform;

(c) status of any other regulatory licence or approval granted to the person by any other financial services regulator;

(d) ability of the person to carry on the regulated activity competently, honestly and fairly; and

(e) reliability of —

- (i) in case of a natural person, that individual person; or
- (ii) in case of a company, the company, its directors, chief executive, management and any substantial shareholder of the company.

(2) Without prejudice to the generality of subsection (1), the Authority shall, in considering whether a person is a fit and proper—

(a) have regard to whether that person-

- (i) has contravened the provision of any law, in Kenya or elsewhere, designed for the protection of members of the public against financial loss due to dishonesty or incompetence, or malpractice by persons engaged in transacting with marketable securities;
- (ii) was a director of a licensed person which has been liquidated or is under liquidation or statutory management;
- (iii) has taken part in any business practice which, in the opinion of the Authority, was fraudulent, prejudicial to the market or public interest, or was otherwise improper or would otherwise discredit the methods of conducting business;
- (iv) has taken part or has been associated with any business practice which casts doubt on his competence or soundness of judgment; or
- (v) has conducted himself in a manner likely to cast doubt on his competency and soundness of judgment;

(b) take into account any information in the possession of the Authority, whether provided by the applicant or not, relating to —

(i) any person who is to be employed by, associated with, or who will be acting for or on behalf of, the applicant in a licensed activity;

(ii) where the applicant is a company in a group of companies-

(A) any other company in the same group of companies;

- (B) any substantial shareholder or officer of the company or any company referred to in paragraph (a);
- (C) whether the applicant has established effective internal control procedures and risk management systems to ensure its compliance with all applicable regulatory requirements; and
- (D) the state of affairs of any other business which the person carries on or purports to carry on.

(3) For the purposes of this section, "group of companies" means any two or more companies one of which is the holding company of the other.

(4) The Authority shall give a person an opportunity to be heard before determining if that person is fit and proper for the purposes of this Act or not.

Repeal and replacement of section 5 of Act No. 4 of 2000.

6. The principal Act is amended by repealing section 5 and replacing it with the following new section-

Grant of a license.

5. (1) The Authority may, in writing, subject to such conditions or restrictions as it may consider proper to impose, license a company as a central depository, if it is not contrary to public interest to do so and the Authority is satisfied that the company—

- (a) has and maintains at all times, such minimum paid-up capital as may be prescribed by the Authority from time to time;
- (b) has a board of directors constituted in accordance with such criteria as the Authority may prescribe;
- (c) shall provide, as far as is reasonably practical, fair, transparent and efficient arrangements for the deposit, registration and transfer of securities;
- (d) shall manage any risks associated with its business and operations prudently;
- (e) shall ensure the compliance of its rules by its agents;
- (f) has made sufficient central depository rules to address the matters prescribed in section 5A;

- (g) has sufficient financial and human resources and the infrastructure to —
- (i) establish and operate a fair, transparent and efficient clearing facility;
- (ii) meet contingencies, including events such as technical complications occurring with an automated system or disasters and its integration with any connected trading systems; and
- (iii) has provided adequate security arrangements.

(2) The Authority shall give a person an opportunity to be heard before declining to grant a licence.

(3) Subject to the provisions of this Act, a central depository licence shall, until it is revoked or suspended by the Authority, be valid.

Insertion of section 5A in Act No.4 of 2000.

7. The principal Act is amended by inserting the following new section immediately after section 5-

Rules of a central depository.

5A. (1) A central depository shall make CDS Rules providing for —

- (a) deposit, registration and transfer of securities;
- (b) settlement of transactions involving securities;
- (c) the proper regulation and efficient operation of the clearing facility which it operates;
- (d) its default process;
- (e) the establishment of a settlement guarantee fund;
- (f) the qualifications for appointment of central depository agents;
- (g) the proper regulation and supervision of its agents;
- (h) the exclusion from participation as central depository agents of persons who are not fit and proper;
- (i) the expulsion, suspension or disciplining of a central depository agent;

- (j) the carrying on of the business of a central depository, having regard to the interests and protection of the investing public; and
- (k) such other matters as the Authority may direct.

(2) A central depository shall submit the rules made under subsection (1) to the Authority for approval.

(3) A licensed central depository shall not amend, vary or rescind its Rules without prior approval of the Authority.

Default process Rules.

5B. The default process rules made under section 5A(1)(d) shall provide for the actions which a central depository may take against a central depository agent that has failed, or has become unable or is likely to be unable to meet its obligations for all unsettled or open market contracts to which it is a party and shall in particular to -

- (a) enable the settlement of all the defaulter's contracts;
- (b) provide, for the purpose of paragraph (a), such sum of money payable by or to the defaulter, in relation to each contract, if this is required after taking into account all the rights and liabilities of the defaulter under or in respect of the contracts in question;
- (c) enable all sums of money payable by or to the defaulter as determined in accordance with paragraph (b) to be aggregated or set-off to produce a net sum, if any, payable by or to the defaulter;
- (d) provide, if any, the net sum referred to in paragraph (c) is payable to the defaulter, that all property of the defaulter which is either subject to a market charge or which has been provided as market collateral shall cease to be subject to the market charge, without prejudice to any other form of charge to which it may be subject, or to be market collateral, without prejudice to its provision as any other form of collateral, as the case may be; and
- (e) provide for the certification by the central depository, of any net sum referred to in paragraph (c) payable to the defaulter, or of any further net sum referred to in paragraph (d) payable by or to the defaulter, as the case may be, or if there is no such sum, the certification by the central depository of that fact.

(4) Where a central depository commences a default process, all subsequent action taken under its rules for settlement of market contracts

to which the defaulter is party, shall be treated as taken under the default rules.

Net sum payable on completion of default measures.

5C. (1) This section shall apply to any net sum certified by a central depository as payable by or to a defaulter, upon the completion of default measures.

(2) Where a receiving or winding up order has been made, or a resolution for the voluntary winding up has been passed, any net sum shall be —

- (a) provable in bankruptcy or winding up proceedings; and
- (b) taken into account for the purpose of any rule of law relating to set-off.

(3) For the purposes of subsection (2), a certificate of a central depository on the amount of the net sum payable, shall be sufficient proof of the net sum payable.

Central depository to prepare and submit report.

5D. (1) A central depository shall, upon completion of default measures, prepare a report containing the-

- (a) action taken against the defaulter; and
- (b) net sum, if any, certified by the central depository to be payable by or to the defaulter.

(2) A central depository shall submit a report made under subsection (1) to the-

- (a) Authority;
- (b) any relevant securities exchange; and
- (c) defaulter to whom the report relates.

(3) The Authority may publish, in such manner as it may consider appropriate, the contents of a report received under subsection (2) for the attention of creditors.

(4) Upon receiving a report made under subsection (2) the defaulter shall, at the request of any creditor —

(a) avail the report to the creditor for inspection within two days from the receipt of such request; or

(b) supply to the creditor, on payment of a prescribed fees, all or any part of the report as requested.

Repeal and replacement of section 8 of Act No. 4 of 2000.

8. The principal Act is amended by repealing section 8 and replacing it with the following new section-

Duties of a central depository

8. (1) A central depository shall —

- (a) establish and operate facilities for the handling of securities centrally;
- (b) ensure that facilities under paragraph (a) provide fair, transparent and efficient depository, clearing and settlement arrangements for securities deposited and any transactions relating to securities cleared or settled through its facilities;
- (c) ensure adequate measures to prevent and mitigate fraud or any other system manipulation mechanisms are established to-
 - (i) ensure safe custody of certificates and other documents deposited with the central depository;
 - (ii) guard against falsification of the records or accounts required to be kept or maintained under the Act; and
 - (iii) ensure a proper and efficient system for the tracing, verification, inspection, identification and recording of all transactions with the central depository;
 - (iv) seek approval for any fees proposed to be levied in respect of the services it renders; and
 - (v) ensure that the risks associated with its business and operations are managed prudently.

(2) A central depository shall, in discharging its duty under subsection (1), act in the interest of the investors and the public.

(3) A central depository shall operate its facilities and perform its

duties in accordance with the rules approved by the Authority under section 5A.

(4) A central depository shall formulate and implement appropriate procedures to ensure that the agents it appoints under section 9 comply with its rules.

(5) A central depository shall, in the conduct of its business, at all times, maintain —

- (a) adequate and properly equipped premises;
- (b) competent personnel; and
- (c) automated systems with adequate capacity and facilities, security arrangements and technical support to meet contingencies or disasters, approved by the Authority.

(6) A central depository shall preserve confidentiality with regard to the information in its possession concerning its central depository agents and their customers:

Provided that such information may be disclosed to the Authority when requested to do so in writing, or upon written request of a securities exchange, for which it is a central depository, or is required to do so by any law.

(7) A central depository shall, immediately notify the Authority if it becomes aware —

- (a) of the inability of any of its central depository agents, to comply with any rule of the central depository;
- (b) of a financial irregularity or other matter which, in the opinion of the central depository, may indicate that the financial standing or integrity of a central depository agent is questionable; or
- (c) of the likelihood of a central depository agent not being able to meet its legal obligations.

(8) A central depository shall be entitled to charge such fees for its services and facilities as may be approved by the Authority.

(9) The Authority may, from time to time, prescribe such other duties to be performed by a central depository as it considers appropriate.

Amendment of section 9 of Act No. 4 of 2000.

9. Section 9 of the principal Act is amended in subsection (2) by deleting paragraph (a) and substituting therefor the following new paragraph-

- (a) any trading participant of a securities exchange for which it is its central depository; or

Insertion of section 10A in Act No. 4 of 2000

10. The principal Act is amended by inserting the following new section immediately after section 10 - .

Property deposited with central depository.

10A. Where a central depository agent, deposits any property as a market collateral with a central depository in accordance with its rules, no action, claim or demand, either civil or criminal, in respect of any right, title or interest in such property shall lie, or be commenced or allowed against a central depository or its nominees, notwithstanding any other provision of the law.

Insertion of new section in Act No. 4 of 2000

11. The principal Act is amended by inserting the following new section immediately after section 12-

Disciplinary action and review of a disciplinary action.

12A. (1) A central depository may reprimand, fine, suspend, expel or otherwise take any disciplinary action against a central depository agent in accordance with its rules.

(2) A central depository shall, within seven days of any action taken under subsection (1), notify the Authority, in writing, giving particulars including the name of the person, the reason and the nature of the action taken.

(3) The Authority may, on its own motion or on application by an aggrieved person, review any disciplinary action taken under subsection (1), and may affirm, modify or set aside the decision of a central depository after giving the central depository and the central depository agent an opportunity to be heard.

(4) Nothing in this section shall preclude the Authority, in any case where a central depository fails to act against a central depository agent, from suspending, expelling or otherwise taking disciplinary action against a

central depository agent:

Provided that the Authority shall give the central depository and the central depository agent an opportunity to be heard.

(5) Any action taken by a central depository under subsection (1), shall not prejudice the power of the Authority to take such further action as it considers necessary against a central depository agent.

Amendments of section 33 of No. 4 of 2000.

12. Section 33 of the principal Act is amended by-

(a) deleting subsection (2) and substituting therefor the following new subsection -

(2) A central depository shall, within three months after the end of its financial year, submit to the Authority an annual report which shall include-

- (a) a copy of the report of the audit conducted under subsection (1), duly certified by the auditors;
- (b) a description of the activities undertaken by the central depository in that financial year;
- (c) the resources, including financial, technological and human resources which the central depository had available, and used, in order to ensure compliance with its obligations; and
- (d) an analysis of the extent to which the central depository considers that the activities undertaken, and resources used, have resulted in full compliance of its obligations.

(b) deleting subsection (3) and substituting therefor the following new subsection-

(3) A central depository shall, at the end of each financial year, subject its operations to an independent audit.

(c) inserting the following new subsections immediately after subsection (3)-

(4) A central depository shall appoint an independent auditor for the purposes of subsection (3).

(5) A central depository shall inform the Authority of the appointment of an auditor under subsection (4).

(6) The auditor shall-

- (a) have a right of access, at all reasonable times, to all operational records and systems of the central depository and is entitled to require from officers of the central depository such information and explanations as the auditor considers necessary for the performance of his duties;
- (b) have a right of access at all reasonable times, to the offices, operation records and systems of all the central depository agents of that central depository;
- (c) prepare a report on the operational capabilities of the central depository system and a statement on whether, in the opinion of the auditor, the central depository system operates and performs its functions satisfactorily with regard to the duties of the central depository.
- (d) submit the report prepared under paragraph (c) to the central depository and a copy to the Authority within ninety days of his appointment.

Insertion of section 43A in Act No. 4 of 2000.

13. The principal Act is amended by inserting a new section immediately after section 43 as follows-

Default process of a central depository to take precedence over laws of insolvency .

43A. The following shall not to any extent be invalid at law on the ground of inconsistency with the law relating to the distribution of the assets of a person on insolvency, bankruptcy or winding up, or on the appointment of a receiver over any of the assets of that person -

- (a) a market contract;
- (b) the rules of a central depository relating to the settlement of a market contract;
- (c) any process or action taken under the Rules of a central depository relating to the settlement of a market contract;
- (d) a market charge;
- (e) the default rules of a central depository; or

(f) any default process.

Insertion of sections 59A, 59B, 59C, 59D and 59E in Act No. 4 of 2000.

14. The principal Act is amended by inserting the following new sections immediately after section 59-

Emergency powers of the Authority.

59A. (1) The Authority may, where it has reason to believe that-

- (a) an emergency exists;
- (b) it is necessary or expedient to protect investors; or
- (c) it is in the interest of the public,

direct a central depository, by notice in writing, to take such action as it may consider necessary including —

- (i) altering the conditions of delivery of securities;
- (ii) fixing the settlement price for liquidation of securities;
- (iii) requiring margins or additional margins for any securities; and
- (iv) modifying or suspending any rules of a central depository.

(2) The Authority may, where a central depository fails, within a specified period, to comply with a direction given under subsection (1) —

- (a) set an emergency margin level in any securities or class of securities; or
- (b) take such other action, as the Authority considers necessary to maintain or restore fair, transparent and efficient clearing and settlement of transactions in securities.

(3) In this section, "emergency" means —

- (a) any act of the Government affecting securities;
- (b) any other major market disturbance which prevents the market from accurately reflecting the forces of supply and demand of securities;

- (c) a threatened or actual market manipulation; or
- (d) any other situation or practice which, in the opinion of the Authority, constitute an emergency.

Authority may issue directions to a central depository.

59B. (1) The Authority may, by notice in writing, if it considers it necessary or expedient -

- (a) to ensure fair, orderly and expeditious clearing and settlement of transactions in securities;
- (b) to ensure integrity and proper management of systemic risks in securities markets; or
- (c) in the interest of the public or for the protection of investors,

issue a general or specific direction to a central depository.

(2) Without prejudice to the generality of subsection (1), any direction issued may relate to —

- (a) clearing and settlement of securities contracts and making adjustments of a contractual obligation arising out of a securities contract;
- (b) the manner in which a central depository carries on its business; or
- (c) any other matter that the Authority may consider necessary for the proper discharge of its functions under this Act.

Authority may appoint an auditor.

59C. (1) The Authority may, if it is satisfied that it is in the public interest to do so, appoint, in writing, an auditor to examine, audit, and report, either generally or in relation to any matter, on the books, accounts, records and the system of a central depository.

(2) A central depository shall meet the expenses of an auditor appointed under subsection (1).

Revocation of a licence.

59D. (1). The Authority may, by notice in writing, revoke a licence granted to a central depository under this Act if a central depository—

- (a) ceases to operate the clearing facility that it had been licensed to operate;
- (b) is being wound up;
- (c) fails to comply with any requirement of this Act;
- (d) fails to comply with a direction of the Authority;
- (e) fails to provide the Authority with information when required to do so;
- (f) provides false or misleading information;
- (g) is operating in a manner that is detrimental to the public interest;
or
- (h) requests the Authority to do so.

(2) For the purposes of subsection (1), a central depository shall be considered to have ceased operation if it has not operated its central depository facility for more than thirty days without the prior approval of the Authority.

(3) The Authority may permit a central depository to, on or after the date on which the revocation is to take effect, continue its operations or carry on such activities affected by the revocation as the Authority may specify for the purpose of —

- (a) winding up its operations; or
- (b) protecting the interest of the public.

(4) The Authority shall not, except where responding to a request under subsection (1) (h), revoke a central depository license without first giving the central depository an opportunity to be heard.

(5) The Authority shall publish in the Gazette any license revoked under this section.

Effect of a revocation.

59E. A revocation under section 59A shall not—

- (a) avoid or affect any agreement, transaction or arrangement which was entered into before the revocation;

- (b) affect any right, obligations or liability arising under such agreement, transaction or arrangement.

Insertion of Part VIII A in Act No. 4 of 2000.

15. The principal Act is amended by inserting a new Part immediately after Part VIII as follows —

PART VIII A - CENTRAL DEPOSITORY SETTLEMENT GUARANTEE ARRANGEMENTS.

Obligation to have approved settlement guarantee arrangements

60A. A central depository shall, as a condition to its licence, subject to the approval of the Authority, establish adequate arrangements to guarantee the settlement of all transactions relating to securities through its system.

Establishment of Central Depository Guarantee Fund.

60B. (1) A central depository may, in fulfillment of the requirements of section 60A, establish a Central Depository Guarantee Fund (hereinafter referred to as "the Fund") for the settlement of trade through the central depository,

(2) The Fund shall consist of—

- (a) a variable risk based contribution, to be determined by the central depository, in consultation with the Authority, and payable by central depository agents who are involved in settlement;
- (b) all penalties and fines imposed by a central depository under this Act;
- (c) such sums of money as may accrue from interest and profits from investing moneys of the Fund;
- (d) such revenue from contributions of a central depository as its Board of Directors may, from time to time, determine; and
- (e) such other funds as the Board of the central depository may, with the approval of the Authority, determine.

Management of the Fund.

60C. (1) A central depository shall manage the Fund established

under section 60B as a separate fund and disclose it as such in the annual balance sheet of the central depository.

(2) A central depository shall keep proper accounts and records of the Fund and shall, in each financial year, prepare a statement of accounts showing the financial position of the Fund in its annual report.

(3) The accounts under subsection (2) shall include all sources of income and contributions to, expenses or disbursements of the Fund and any investments of the Fund.

(4) The accounts and records of the Fund shall be audited by the auditor appointed by the central depository to audit its annual accounts.

(5) The central depository shall make Rules for the operation and maintenance of the Fund.

Insertion of new section in Act No. 4 of 2000.

16. The principal Act is amended by inserting the following new section immediately after section 63—

Insurance

63A. (1) A central depository shall, at all times, maintain an insurance policy to cover loss or damage arising from such occurrences as may be prescribed from time to time by the Authority.

(2) A central depository shall obtain and maintain, at a reasonable and competitive cost, one or more insurance policies for such amounts and coverage as may be determined by the central depository in its interests and in the interest of its depositors.

(3) The Authority or a central depository agent may inspect the insurance policies maintained under subsection (2) during business hours.

(4) A central depository shall notify the Authority and the central depository agents of any reduction in the coverage or amount of any policy of insurance it maintains.

