



Capital Markets Project

## SUGGESTIONS FOR IMPROVING SRO GOVERNING INSTRUMENTS

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### BACKGROUND

- USAID Capital Markets Project Consultant's Report includes review and commentary on the governing instruments of SROs that requested such a review and are candidates for sole SRO status under the SRO provisions of the 2006 law
- To date, the following SROs' governing instruments, including membership requirements, rules of fair practice, codes of ethics, disciplinary and arbitration procedures, have been reviewed:
  - PARD\*
  - PFTS Association
  - UAIB
- Governing instruments of Interbank Currency Exchange, Regional Stock Union – Perspektiva, and Ukrainian Stock Exchange also are being reviewed

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\* APSM declined to meet with CMP representatives.

## METHODOLOGY – PRELIMINARY VIEWS

- Written comments are being provided to individual SROs. Meetings will be held separately with each SRO to review and discuss the comments
- This presentation is intended only to address some of the common issues that were encountered during the review
- The three sets of SRO documents reviewed to date are generally well-prepared and provide a foundation for self-regulation.
- It is likely that the greater challenges in achieving robust self-regulation will be sufficient SRO resources and building membership consensus

## ASSOCIATED PERSONS OF SRO MEMBERS SHOULD BE SUBJECT TO SRO REGULATION

- Issue was discussed in my morning presentation. I recommend a contractual solution. If this cannot be achieved, a legislative solution is essential
- Securities regulation in Ukraine will not be effective either via direct SSMSC regulation or via SRO regulation until it is recognized that both the SSMSC the SROs need authority to regulate and discipline all associated persons of their member firms.

## STRONGER PROVISIONS TO BIND SRO MEMBERS AND ASSOCIATED PERSONS

### **Model member firm provision:**

By its signature below, the undersigned member firm (firm), as a condition and in consideration of its becoming a member of [insert name of SRO] (SRO), submits to the authority of the SRO and agrees to comply, and use its best efforts to ensure that all associated persons of the firm comply, with all requirements of the governing instruments, rules and procedures of the SRO. The undersigned firm further agrees to be comply with all rulings, orders, directives and decisions of, and disciplinary sanctions imposed by the SRO, subject to right of appeal or review as provided by law.

## STRONGER PROVISIONS - continued

### **Model Associated Person Provision:**

By my signature below, and as a condition and in consideration of my employment by [insert name of member] (member) and member's becoming a member of [insert name of SRO] (SRO). I submit to the authority of the SRO and agree to comply with all requirements of the governing instruments, rules and procedures of SRO. I further agree to comply with all rulings, orders, directives and decisions of, and disciplinary sanctions imposed by the SRO, subject to right of appeal or review as provided by law.

## GOVERNANCE OF A SOLE SECURITIES TRADER SRO

- It is possible that the sole securities trader SRO will be a current or new SRO that is affiliated with a securities market
- If so, significant governance issues need to be addressed
  - Members of the SRO should not be required to be members or participants in the affiliated market
  - The SRO's finances must be separate from the markets, so that SRO members' dues do not fund the market's operations; if the market contracts with the SRO for surveillance or market regulation functions, as distinguished from SRO membership regulation functions, the market should pay the SRO for such services
  - Personnel of the SRO responsible for self-regulatory functions should not be the same as personnel of the market
  - The market and SRO should have separate CEOs who report to separate boards, although each board's members may be the same; independent directors might be added over time if qualified
  - One member – one vote principle should apply

## ARTICLE 120 OF THE COMMERCIAL CODE

- For apparent lack of a better alternative, SROs are economic associations under the Commercial Code
- Article 120 provides in part"
  - It must be stated in regulation of association, that it is an economic association. Association does not have a right to interfere in economic activity of enterprises – participants of association
- To effectively function as an SRO, an SRO needs to directly affect it's members' and associated persons' activities. In the extreme case, if a member or associated person seriously violates securities laws or SRO rules, the SRO should have the authority to suspend and/or prohibit member or associated person from participation in the securities industry
- To preclude the possibility of members and associated persons subject to SRO discipline using Article 120 as a defense, Article 120 needs to be amended to clarify that it does not prohibit self-regulation by licensed SROs

## OTHER ISSUES

- An SRO cannot be an effective self-regulator if all of its rules must be approved by its membership, which normally meets only once a year. The SRO's governing instruments should authorize the SRO's Board to adopt most SRO rules
- All personnel of the SRO should be subject to a code of conduct that includes provisions regarding confidentiality of information and prohibitions on use of nonpublic information
- Publicly available financial statements of all SROs should be prepared in accordance with IFRS and subject to external audit by an independent auditor in accordance with ISA

THANK YOU  
QUESTIONS?