

## MINUTES

### FINANCIAL DERIVATIVES ADVISORY COMMITTEE MEETING

Date: 06 March 2018  
Time: 10h00  
Venue: Ubuntu Conference Room – 1st Floor, JSE Offices, Sandown

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Present: Donna Nemer (DN), Guy Algeo (GA), Leanne Parsons (LP), Matthew Arnott (MA), Ved Somera (VS), Langa Manqele (LM), Godfrey Matjuda (GM), Andre Koen (AK), Cameron Petersen (CP), Helen Masson,

Apologies: Aveshen Pillay (AP), Brendan Harcourt-Wood (BHW), Eben Mare (EB)

Dialled In: Gavin Betty (GB), Shiran Samuels (SS), Petrus Bosman (PB), Naval Singh (NS), Phillip Dube (PD), Matthew Arnott (MA), Bryan MacCallum (BM), Bryan Hatty (BH)

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#### 1. WELCOME AND APOLOGIES

DN welcomed all the attendees to the first Financial Derivatives Advisory Committee (FDAC) meeting for 2018.

#### 2. CONFIRMATION OF PREVIOUS MINUTES

The minutes of the previous FDAC meeting were confirmed and accepted as correct.

#### 3. FEEDBACK ON MATTERS ARISING

##### 3.1. Marked-to-Market on DTOP and DCAP

- Valuations team is monitoring, collecting and cleaning up on-screen data.
- This exercise will be carried over up to FCO (15<sup>th</sup> March), the results we will be share the results with FDAC on the week after FCO.

##### 3.2. WMCO

- A comparison between WMCO and ZAR=D3 has been done based on the available Reuters data.
- The comparison shows the spreads between WMCO and ZAR=D3 over the period 21 August 2017 to 20 November 2017
- The implementation of WMCO in production will be dome after ITaC go-live.

#### 4. ITAC PROJECT UPDATE

LP informed the committee that the JSE has issued a market notice relating to the upcoming market dress rehearsal. LP alluded that, currently the JSE has been busy with mandatory clearing member testing (MCMT) to ensure consistency of post trade activities before bringing the entire market into this testing. The MCMT cycle 2 testing was rescheduled, as agreed with clearing members to run from 5th March to the 16th March 2018 as an end-to-end testing with full position take-on. The MCMT cycles that are earmarked will run up-to 5-cycles. With current MCMT cycle 2 testing, there has been some challenges relating to clearing member software not performing to the required standard, and also not working efficiently enough to engage the entire market for testing. The clearing member software provider has informed the JSE that their issues on software readiness are being resolved and a further release from their side will be delivered on 19 March 2018 before the planned market dress rehearsal testing date.

The next mandatory market facing dress rehearsal (MMDR) which is mandatory for trading members, software providers and all shared infrastructure providers (SIPs) is scheduled for Saturday, 24 March 2018. The MMDR is a functional testing session that will simulate the normal production trading day. It is about testing all business processes impacted by the new solutions such as orders, trades and deal management functions to verify the outcome of the results on all screens and reports including any downstream integration etc. The trading members should note that it is not a high volume testing but a test that focuses on verifying integrity and accuracy. LP advised the trading members that the upcoming dress rehearsal on the 24th March 2018 is the last opportunity for trading members to test with multiple software providers as they need to finalise their choices to ensure sufficient time for roll out and readiness within their organisations. The dress rehearsal testing emphasis is mainly about testing connectivity with the JSE or SIPs, ensuring their chosen software meets their business requirements and to familiarise themselves with chosen solutions/front ends.

To date there has been three categories of issues raised:

- Commissions functionality
- Market Making,
- Deal Management

Software providers have informed the JSE that they have fixed bugs relating to commissions and deal management. This means that the trading member can test on CTS prior to the upcoming dress rehearsal testing or even post that. Regarding market making functionality, the JSE has asked members to engage with their software providers to find out how it would function in an ITAC world and how they could test this in CTS.

The JSE is willing to help trading members that come forward for assistance with specific individual software provider but will not be able to choose software providers for trading members.

The JSE implemented the cost assistance programme and credits on members invoices commenced end Jan 2018.

The JSE will send the test pack check list to compliance offices and ITaC responsible officers a week prior to dress rehearsal testing and would also request feedback from members post testing. LP mentioned that trading members do not pay for CTS and members need to engage with their software providers to be able to test in CTS. LP informed the committee that some of terminology will be changing in ITAC go-live therefore additional documents will be sent out to trading members to assist with client education and readiness.

It was noted that the go-live date is highly depended on the dress rehearsal outcome and the result of MCMT. The JSE will engage with clients on a targeted go-live date during April 2018.

## 5. OD TRADE ACTIVITY AND TRADE RULE

### OD Trade definition

A delta trade is a transaction where a member trades as an agent or a principal in a single equity security where the transaction transfers the delta hedge:

- 6.40.4.1 from one member to another member; or
- 6.40.4.2 from a client of a member to that member; or
- 6.40.4.3 from a client of a member to another member.

in respect of a derivative transaction which has been reported to either the JSE derivatives trading system or the derivative trade recording system referred to in the directives.

### Background on Zero Fees for OD Trades

The JSE, along with the market, agreed to zero fee the OD trade type in January 2016 to avoid a the duplicate charge. The zero fee is an automated and upfront process, there is no validation of OD Trade against the OD Trade definition prior applying a zero fee. This automated and upfront zero fee is not a common JSE practice, other booking fees are charged first and upon a member's request a zero fee would be effected after checking the qualification criteria.

### Auditor's review

The automated and upfront zero fee has been flagged by our external auditors as a concern that JSE has no controls in place to ensure that a zero fee is applied to OD trades that strictly meet the OD trade definition. Auditors have recommended that JSE puts measures to validate the accurate use of the OD trade type and conduct regular commercial audits on the process.

### Next Steps

- Update current OD definition and Zero Fee parameters
- Members to send JSE a monthly report on OD trades that warrant a Zero Fee.

### Required information:

- The JSE ticker
- OD trade details
- Derivative trade details.
- Original Stock trade details

- Original Stock Trade  $\leq$  48 Hours

The information will be collected and analysed to establish whether the function is used correctly. If a member is not using the function correctly the JSE would in turn charge the required fees to the member.

It was raised by a committee member that JSE members should be more concerned about being in contravention of the JSE rules rather than whether they had paid fees or not. Committee members also raised that there would be additional resources required to send through the information and would need to discuss with the JSE on how to best archive this function. A working group will be setup to discuss with the members the OD trade type rule and how to best validate the use of the function.

## **6. TREATMENT OF CORPORATE ACTIONS (ROUNDING RULES)**

AK informed the committee that a few market makers have raised a concern on how certain corporate actions; specifically special dividends are treated. Certain clients are benefited whilst the market makers lose money. Due to the nominal size of single stocks, there will always be rounding issues and as a result, certain market participants will lose or make money. AK then invited the committee to make suggestions as to how to treat corporate actions

A committee member highlighted the need to address these issues as it's not only market makers who make a loss but clients too. In order to find the most suitable solution, the committee agreed to formulate a workshop to address this issue.

## **7. ALSI TOP 40 ON CME GLOBEX (EXTENDED HOURS)**

DN shared with the committee that the JSE recently had discussions with the CME about the arrangement that they have with the Korean stock exchange. The Korean index futures trades on the CME after hours and then those positions are put back on the Korean exchange in the morning and an end of day process is then run, in effect, translating into extended trading hours. DN then went on to mention that she will be meeting with the Korean exchange to ascertain if this arrangement is worthwhile. The CME is willing to do a similar setup for the JSE; however, the JSE is not willing to do so unless it is beneficial for both markets. She added that the JSE would not want to take liquidity away from the JSE but will consider such an arrangement if it will result in additional liquidity and extended trading hours for JSE market participants.

A committee member made a comment that Korea does not really have a time overlap with the US, unlike the South African market which does and this may result in volumes being taken away from our market. The committee member added that if the contract is denominated in dollars then it may result in arbitrage. International banks may benefit as they have trading lines to the CME whereas the local brokers may be disadvantaged as they do not have trading lines into the CME. A further comment was made that the arrangement could work if there are committed market makers. Another comment was made by a committee member that the JSE should focus on finalizing ITAC and improving liquidity on the local market. When ITAC goes live, the JSE could then implement a liquidity provider and market making scheme. After much deliberation it was agreed that the JSE park the idea for now and revisit it at a later stage.

## **8. GENERAL**

The JSE will be looking at tripartite agreements in the Equity derivatives markets. There is no current commitment on this issue but the JSE will be looking at the fees and discounts in this market just as there are discounts in other markets.