

# How Capital Markets are Formed and Regulated in Ethiopia

## Description

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Capital Market has been defined as a market where securities such as shares or equities, bonds, derivatives or other related securities are bought and sold. Capital Market Proclamation No 1248/2021 (this Proclamation hereafter) has been issued to regulate the capital market as of July 2021. Overview of the main concepts of the capital market organs and objectives will be dealt briefly.

## Ethiopian Capital Market Authority

The Ethiopian Capital Market Authority (ECMA hereafter) is established by this Proclamation as an autonomous Federal Regulatory authority. One of the major objectives of ECMA is to ensure the existence of a capital market environment in which securities can be issued and traded in an orderly, fair, efficient manner. ECMA, as a regulatory authority, grants licenses to any person to operate as a security exchange, derivative exchange, security depository and clearing company, capital market service provider, over-the-counter trading facility or any other activity deemed by ECMA as a regulated activity under its jurisdiction. ECMA shall take administrative measures for the breach of provisions of this Proclamation or regulations and directives issued hereunder. ECMA regulates and oversees trading in primary and secondary markets of securities, the use of electronic trading platforms that deal with securities and give recognition and oversee the activities of self-regulatory organizations. ECMA is accountable to the Prime Minister of Ethiopia.

## Self Regulatory Organizations

Self Regulatory Organizations(SRO) are entities that are recognized under this Proclamation to regulate their own members through the adoption and enforcement of rules of conduct for fair, ethical and efficient practices in the capital market. SRO envisions conducting their business with a view to promoting and protecting investors and the public interest. SROs that intend to be recognized and allowed to operate need to apply to ECMA for recognition and operation. Upon acceptance, the SRO shall be declared as an SRO entity with delegated powers. The SRO shall submit its annual report to the ECMA.

## The Ethiopian Security Exchange

The Ethiopian Security Exchange (ESE) is established as a share company by this Proclamation. The shareholders of the ESE shall be the Government of Ethiopia on one hand and on the other private investors including foreign investors. The total ownership of the Government or state-owned entities shall not exceed 25% of the ESE capital. ECMA shall grant an exchange license to the ESE upon meeting the minimum capital requirement and other requirements specified by ECMA. Security exchange has been defined in this Proclamation as a place which constitutes, maintains or provides a market or a facility by means of which offers to sell, purchase or exchange securities are regularly made or accepted.

### **Private Security Exchange Share Companies**

ECMA will grant licenses for other security exchange and trading platforms that are established as share companies

### **Security Depository and Clearing Company**

Security Depository and Clearing Company (SDCC) is defined as any legal entity that offers security depository, clearing and settlement and other related services. The SDCC license is granted to a share company that meets the minimum capital requirement and other requirements of the ECMA. The main obligation of SDCC is to arrange for fair and effective clearing and settlement in relation to any commercial transaction of securities including repo agreement (repurchase agreements) and securities lending. Public companies and other issuers of securities shall register the type of their securities and information on the owners of the securities at the Central Securities Depository.

### **Government Securities**

The National Bank of Ethiopia (NBE) shall have autonomous power to establish, own, operate and participate and regulate central security depository for government securities. ECMA may authorize the NBE to provide securities depository and clearing services to private securities traded at the securities exchange.

### **Capital Market Service Providers Licencing**

Capital market service providers are required to acquire a capital market services license. Licensed activities include securities broker, investment advisor, collective investment scheme operator, investment bank, securities dealer, custodian, market maker, credit rating agency, appointed representative of a capital service provider and any other person who conducts or participates in any activity in securities.

### **Public Offering and Trading of Securities**

A publicly traded security is required to be registered by ECMA, prior to the offer or placement. The issuer of securities is required to prepare prospectus and approval of such prospectus is required by ECMA. Here the 'issuer' is defined in this Proclamation as a person who issues or proposes to issue any security. These include the government, company or other legal entity that offers securities to the public. Privately issued securities shall not be traded publicly. An offer of asset backed securities shall be made only if they are issued by a special purpose institution.

### **Collective Investment Schemes**

Collective Investment Scheme(CIS) is an arrangement formed for the purpose of providing facilities for persons to participate in or receive profits or income arising from the acquisition, holding management or disposal of securities or any other property or sum paid out of such profits or income. The scheme's assets are managed by a person who is responsible for management of the scheme's assets and client accounts. Investors who participate in the arrangement do not have day-to-day control over the management of the scheme's assets.

CIS may be established as investment companies such as mutual funds, limited partnerships or other forms under the Commercial Code. The CIS has to be registered by ECMA. CIS can be managed by collective investment scheme Operator. The Operator is a legal entity that has the over all responsibility for management and performance of the functions of the CIS.

### **Prohibited Trading Practices**

Insider trading, market manipulation, false trading, fraudulent transactions, front-running and similar other trading practices are some of the prohibited trading practices listed in the Proclamation.

### **Compensation Fund**

Compensation fund is established by the Proclamation for the purpose of granting compensation to investors who suffer monetary loss resulting from the failure of a capital market service provider or securities exchange to meet his contractual obligations and paying beneficiaries from collected unclaimed dividends when they resurface.

### **Criminal Liability and Administrative Measures**

The Proclamation incorporates different fines and imprisonment for violations of the Proclamation. ECMA also imposes administrative measures such as revoking or suspending licenses, senior personnel or board of directors.

### **Capital Market Tribunal**

The Capital Market Tribunal is established by this Proclamation to hear appeals against decisions of ECMA. A party who is dissatisfied by the decisions of the tribunal may within 30(Thirty) days after being served with notice of the decision, file a notice of appeal on questions of law only, to the Federal High Court.

### **Settlement of Disputes**

Disputes among parties involved in the capital market concerning any civil matter arising under this Proclamation shall be resolved by mediation first and then by arbitration. The decision of the arbitration panel shall be final and binding on the parties.

## **Conclusion**

Capital markets are established to support the development of the national economy through mobilization of capital, promoting financial innovations and sharing investment risks. A legal framework that regulates and supervises capital markets is adopted by this Proclamation. The rules enshrined in the Capital Market proclamation are intended to ensure capital markets are operated fairly, with integrity and efficiency.

For more information and inquires you may contact us at [info@dmethiolawyers.com](mailto:info@dmethiolawyers.com)

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### **Date Created**

March 13, 2022

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