

**Nigeria: Publication of Financial Sector Assessment Program Documentation—  
Detailed Assessment of Implementation of IOSCO Objectives and Principles of  
Securities Regulation**

This Detailed Assessment of Implementation of IOSCO Objectives and Principles of Securities Regulation for Nigeria was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed in May, 2013. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Nigeria or the Executive Board of the IMF.

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

Copies of this report are available to the public from

International Monetary Fund • Publication Services  
700 19<sup>th</sup> Street, N.W. • Washington, D.C. 20431  
Telephone: (202) 623-7430 • Telefax: (202) 623-7201  
E-mail: [publications@imf.org](mailto:publications@imf.org) Internet: <http://www.imf.org>

**International Monetary Fund  
Washington, D.C.**

FINANCIAL SECTOR ASSESSMENT PROGRAM

# NIGERIA

IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES  
REGULATION

# DETAILED ASSESSMENT OF IMPLEMENTATION

MAY 2013

INTERNATIONAL MONETARY FUND  
MONETARY AND CAPITAL MARKETS DEPARTMENT

THE WORLD BANK  
FINANCIAL SECTOR VICE PRESIDENCY  
AFRICA REGION VICE PRESIDENCY

| Contents   | Page |
|--|------|
| Glossary .....   | 3    |
| I. Summary.....  | 4    |
| II. Introduction .....   | 6    |
| III. Information and Methodology Used for Assessment .....                         | 6    |
| IV. Institutional and Market Structure—Overview .....                              | 7    |
| V. Preconditions for Effective Securities Regulation.....                          | 8    |
| VI. Main Findings.....   | 9    |
| VII. Recommended Action Plan and Authorities’ Response.....                        | 19   |
| A. Recommended Action Plan.....  | 19   |
| B. Authorities’ Response to the Assessment .....                                   | 21   |
| VIII. Detailed Assessment .....  | 26   |
| <br>Tables   |      |
| 1. Summary Implementation of the IOSCO Principles—Detailed Assessments .....       | 12   |
| 2. Recommended Action Plan to Improve Implementation of the IOSCO Principles ..... | 19   |
| 3. Detailed Assessment of Implementation of the IOSCO Principles .....             | 27   |

**GLOSSARY**

|        |  |
|--------|--|
| APC    | Administrative Proceedings Committee                 |
| AGF    | Attorney-General of the Federation                   |
| AMCON  | Asset Management Corporation of Nigeria              |
| ASCE   | Abuja Securities and Commodities Exchange            |
| ASEM   | Alternate Exchange Market                            |
| CAC    | Corporate Affairs Commission                         |
| CAMA   | Companies and Allied Matters Act                     |
| CBN    | Central Bank of Nigeria                              |
| CIS    | Collective Investment Scheme                         |
| CMC    | Capital Market Committee                             |
| CMO    | Capital Market Operator                              |
| CRF    | Consolidated Revenue Fund                            |
| CSCS   | Central Securities Clearing System                   |
| EFCC   | Economic and Financial Crimes Commission             |
| ETF    | Exchange-Traded Fund                                 |
| FMF    | Federal Ministry of Finance                          |
| FRC    | Financial Reporting Council                          |
| FSRCC  | Financial Services Regulation Coordinating Committee |
| ISA    | The Investments and Securities Act, 2007             |
| ISSC   | Information Sharing Sub-committee of the FSRCC       |
| IST    | Investments and Securities Tribunal                  |
| JTF    | Joint Task Force                                     |
| MMoU   | Multilateral Memorandum of Understanding             |
| MoU    | Memorandum of Understanding                          |
| NAICOM | National Insurance Commission                        |
| NASB   | Nigerian Accounting Standards Board                  |
| NIBBS  | Nigerian Inter-Bank Settlement System                |
| NPF    | Nigeria Police Force                                 |
| NSE    | Nigerian Stock Exchange                              |
| PENCOM | National Pension Commission                          |
| SEC    | Securities and Exchange Commission (Nigeria)         |
| SRO    | Self-Regulatory Organization                         |

## I. SUMMARY

- 1. The regulatory framework for securities markets in Nigeria has improved markedly since the 2002 FSAP, and particularly in the last five years.** Since the adoption of the Investments and Securities Act 2007 (ISA) and the first set of rules and regulations of the Nigerian Securities and Exchange Commission (SEC), the regulatory framework has been further strengthened and expanded. It now covers more products and market participants, and has addressed the need to improve the quality and timeliness of disclosures and manage the risks inherent in the management of client assets in collective investment schemes.
- 2. There are comprehensive legal provisions to ensure a robust governance structure for the SEC.** The requirements for qualifications of Board members, the establishment of fixed terms, the confirmation of nomination and removal by the Senate, and the need of a cause to remove a Board member, as opposed to the former practice of Boards being dissolved by the new Executive, provide for a more robust governance structure. However, the SEC has been without a Board since June 2012. In addition, it does not currently have sufficient internal policies, procedures and practices relating to its core functions. These deficiencies jeopardize the proper governance and functioning of the SEC.
- 3. The SEC's independence has improved with the adoption of the ISA, even though certain remaining provisions and practices affect its full independence.** The SEC is self-funded through fees collected from market participants and has the authority to hire its staff and to establish their remuneration. In practice, its dependence on market-based funding creates a need to obtain the resources needed to operate adequately without adding excessive cost to the investors and market participants. The minister of finance has the power to give directives to the SEC, modify or rescind the rules proposed by the SEC and exempt certain persons from the application of the ISA after consultation with the SEC. The last power has been used once. During any period where the SEC is without a Board, the minister of finance must confirm the sanctions imposed by the SEC. Even though the Senate does not have any formal role vis-à-vis the day-to-day operations of the SEC, in practice its views seem to have an impact on the SEC's decisions. The mere existence of these types of legal or practical powers, in particular if they are not transparently exercised, has the potential to undermine the SEC's independence.
- 4. The SEC cooperates both at the domestic and international level with its counterparts and other authorities.** The SEC is a member of the Financial Services Regulation Coordinating Committee (FSRCC). The FSRCC members have signed a Memorandum of Understanding (MoU). The SEC is also a member of the Financial Reporting Council (FRC) established by the FRC Act 2011. The SEC and FRC need to cooperate on financial reporting, corporate governance and auditor independence. The SEC is a signatory to the IOSCO Multilateral MoU (MMoU) and as such it is in a position to fully

assist foreign securities regulators and share information with them. So far it has been requested to provide assistance in a limited number of cross-border investigations.

5. **The overall level of technical expertise in the key functions of the SEC is less than optimal.** The SEC has 17 departments and staff of over 630 people, of which only 30 percent are currently engaged in the core regulatory and supervisory functions. This proportion has increased over the past few years, but the SEC should focus on further increasing it as soon as possible. The coordination in a large organization such as the SEC is challenging, and the current division of responsibilities between the departments seems to create inefficiencies and overlaps. Without sufficient written procedures to serve as guidance and the less than optimal collaboration between the departments, the SEC's discharge of its functions falls short of expectations, mainly in the areas of inspections, investigations and enforcement.

6. **The SEC focuses on regulating the products offered to investors through extensive scrutiny of prospectuses for all securities, including collective investment schemes.** This approach derives from the regulatory framework that emphasizes initial disclosures to investors. Conduct of business requirements for market intermediaries are largely in place, but the regulatory framework is weak in prudential and organizational requirements, including internal control and risk management. Fund managers and issuing houses are covered by the product-related inspections, whereas broker-dealers have been rarely inspected by the SEC. The few inspections made have been primarily triggered by major deficiencies in the broker-dealers' capital levels. The SEC has indicated that the regular inspections have been recommenced after the mission, but the scope and nature of these inspections has not been assessed.

7. **The inadequate regulatory requirements and limited on-site supervision of broker-dealers has the potential of introducing systemic risks to the Nigerian financial system.** This was already experienced during the crisis, and partially addressed through the more stringent requirements on margin lending introduced by the Central Bank of Nigeria (CBN) and the SEC. Due to the weak financial condition of many broker-dealers and limited ongoing monitoring, new risks may arise and remain unaddressed. As in many countries, the securities settlement system is a potential source of contagion. The SEC should promptly implement a major overhaul of the capital requirements applied to broker-dealers, by raising their initial capital requirements and requiring them to maintain sufficient risk-based capital on an ongoing basis. A new, more robust regime would need to include ongoing monitoring and reporting requirements, accompanied by robust enforcement. Early intervention powers of the SEC should be strengthened and effectively applied.

8. **The Nigerian Stock Exchange (NSE) has self-regulatory powers over broker-dealers.** It is required to create and enforce its own rules and report on the results of its self-regulatory activities to the SEC. There is room for improvement in the cooperation and coordination between the SEC and the NSE in broker-dealer supervision. The SEC should

also ensure that the NSE, as an operator of key market infrastructure, is subject to robust ongoing supervision to ensure that the planned changes are introduced in a manner that best contributes to the efficiency, integrity and transparency of the Nigerian securities markets. The respective roles of the SEC and NSE will likely need to be reassessed in the context of the NSE's planned demutualization.

9. **The SEC has comprehensive enforcement powers as provided by the ISA.** It has used them for administrative, civil and criminal actions, but work remains to be done to ensure their effective and consistent use. The departments involved in inspections, investigations and enforcement are not communicating and coordinating adequately. The decisions to take enforcement action are not always adopted in a timely manner. The need to take effective enforcement action is essential for building public confidence in the Nigerian securities markets and its regulator.

## II. INTRODUCTION

10. **An assessment of the level of implementation of the IOSCO Principles in Nigeria was conducted from September 4 to 19, 2012 as part of the IMF-World Bank Financial Sector Assessment Program (FSAP).** The assessment was made by Eija Holttinen, Monetary and Capital Markets Department, IMF, and Carlos Barsallo, MCM expert. The last IOSCO assessment in Nigeria was conducted in 2002.

## III. INFORMATION AND METHODOLOGY USED FOR ASSESSMENT

11. **The assessment was made based on the IOSCO Objectives and Principles of Securities Regulation approved in 2010 and the Methodology updated in 2011.** As has been the standard practice, Principle 38 was not assessed due to the existence of separate standards for securities settlement systems and central counterparties.

12. **The IOSCO Methodology requires that assessors not only look at the legal and regulatory framework in place, but also at how it has been implemented in practice.** The ongoing global financial crisis has reinforced the need for assessors to make a judgment about supervisory practices and to determine whether they are sufficiently effective. Among others, such a judgment involves a review of the inspection programs for different types of supervised entities, the cycle, scope, basis for and quality of inspections as well as how the agency follows up on findings, including by using enforcement actions.

13. **The assessment benefited from a document prepared by the SEC prior to the mission.** It included references to most of the relevant provisions of the ISA and the SEC Rules and Regulations for the majority of the Principles, inserted into the IOSCO self-assessment template. The document did not include information on the supervisory and enforcement policies and practices of the SEC. The staff of the SEC used their best efforts to collect this and other missing information during the mission, and most of the information required for a robust assessment was provided by the end of the mission. The depth of the

assessment of some Principles was impaired by the fact that the primary expertise for those matters lies outside the SEC.

14. **In addition to the SEC, meetings or conference calls took place with staff from the relevant public sector authorities and some market participants.** These included the Economic and Financial Crimes Commission (EFCC) and Financial Reporting Council (FRC), as well as banks, issuing houses, a fund manager, an audit firm, the Nigerian Stock Exchange (NSE), the Central Securities Clearing System Ltd (CSCS), and industry associations (Chartered Institute of Stockbrokers and Association of Stockbroking Houses of Nigeria).

#### IV. INSTITUTIONAL AND MARKET STRUCTURE—OVERVIEW

15. **The only securities exchange currently operating in Nigeria is the Nigerian Stock Exchange (NSE).** Its market capitalization dropped from the end–2008 value of US\$80.6 billion to a low point of US\$27.7 billion, before recovering to US\$52.0 billion at end–September 2012. At end–September 2012, there were 202 listed companies and 311 dealing members at the NSE; however according to the information provided by the NSE only 254 of those dealing members are currently active. Since the beginning of 2010, only six new companies have listed on the NSE. Despite the large number of dealing members, the largest members are responsible for a significant proportion of trading at the NSE. During the first half of 2012, the market share of the 10 largest dealing members was over 75 percent.

| Dealing Member                    | Value of Trading (US\$) | Market Share (%) |
|-----------------------------------|-------------------------|------------------|
| Stanbic IBTC Stockbrokers Limited | 223,451,325.88          | 20.44            |
| Rencap Securities (Nig) Limited   | 197,661,692.14          | 18.08            |
| Chapel Hill Denham Mgt Limited    | 142,633,635.80          | 13.05            |
| CSL Stockbrokers Limited          | 65,837,264.75           | 6.02             |
| A.R.M Securities Limited          | 51,985,160.78           | 4.76             |
| FBN Securities Limited            | 40,206,422.68           | 3.68             |
| Cordros Capital Limited           | 35,787,223.41           | 3.27             |
| Vetiva Capital Management Limited | 34,876,701.85           | 3.19             |
| BGL Securities Limited            | 22,256,980.55           | 2.04             |
| Meristem Securities Limited       | 20,463,608.54           | 1.87             |
|                                   |                         | 76.40            |

16. **In addition to broker-dealers, the market intermediaries operating in the Nigerian securities markets include issuing houses, underwriters, portfolio managers, and investment advisers.** No up-to-date information on the number of active firms and the extent of their business is currently available, since there is no requirement for the firms to

inform the SEC on when they cease to provide the registered functions. In this regard therefore, the information on the SEC website is not reliable.

17. **The collective investment scheme sector remains small.** As at September 7, 2012, the Net Asset Value of the funds under management remained at approximately US\$600 million, managed in only 43 collective investment schemes that were primarily open-ended unit trusts.

| <b>Fund Type</b>   | <b>Number of Funds</b> | <b>Net Asset Value (US\$)</b> |
|--------------------|------------------------|-------------------------------|
| Equity funds       | 20                     | 279,741,387.62                |
| Money market funds | 2                      | 62,777,006.50                 |
| Bond funds         | 4                      | 31,192,910.64                 |
| Real estate funds  | 2                      | 104,741,806.95                |
| Balanced funds     | 11                     | 65,502,462.24                 |
| Ethical funds      | 4                      | 37,996,165.68                 |
| <b>Total</b>       | <b>43</b>              | <b>581,951,739.63</b>         |

#### V. PRECONDITIONS FOR EFFECTIVE SECURITIES REGULATION

18. **The preconditions for effective regulation and supervision of Nigerian securities markets have improved in the last years, but further changes are needed.** Nigeria operates a federal political structure under the Constitution of the Federal Republic of Nigeria, 1999. The development of the Nigerian legal system has been greatly influenced by its colonial past as a part of the British Commonwealth. Other sources of Nigerian law include local legislation (state and federal), Nigerian case law as well as customary law. The principles of judicial precedent and hierarchy of courts is also a fundamental part of the legal system with the Supreme Court of Nigeria at the apex of the court system.

19. **The Companies and Allied Matters Act (CAMA) provides the main framework for the corporate sector.** The CAMA deals with the incorporation and winding-up of companies as well as provisions concerning shares, debentures, meetings and proceedings, directors, financial statements and audit, and dealings in companies' securities. The CAMA also establishes the Corporate Affairs Commission (CAC), with responsibility for administering the Act and establishing and maintaining a companies' registry. The CAMA works reasonably satisfactorily for the present. The CAMA also covers insolvency proceedings of companies and provides for receivers and managers to be appointed, companies to be wound up and arrangements and compromises to be made with creditors. The Bankruptcy Act is based on the comparable U.K. legislation for personal insolvency. The Banking and Other Financial Institutions Act regulates general banking matters, including licensing and supervision.

20. **The FRC Act 2011 replaced the NASB with the FRC as the body with oversight responsibilities in the area of the regulation of financial reporting.** The FRC is responsible for issuing accounting standards as well as monitoring and ensuring the accuracy, veracity and fairness of accounting and financial reports of public interest companies in line with applicable standards. The FRC has developed a roadmap for the adoption of IFRS in Nigeria in 2012.

21. **The Investments and Securities Tribunal (IST) provides a process for the resolution of securities markets related cases that do not have to be resolved in the regular court system.** The IST was established in 2002. Decisions by the IST can be appealed to the Court of Appeal and from it to the Supreme Court. Members of the country's financial sector have criticized the judicial system in relation to delays involved in the determination of cases and the level of corruption in the system. Cases taking 10 to 20 years to resolve are not uncommon. Perception of corruption amongst members of the judiciary, particularly in the lower courts is widespread. The federal government's fight against corruption has resulted in an improvement in the perception of the extent of corruption as indicated by Transparency International in 2011, but corruption continues to be a significant problem. In the case of the SEC, its management has expressed zero tolerance on corruption. However, according to information received from both SEC internal and external sources during the mission, challenges remain in ensuring that the SEC staff meets the high integrity requirements expected from public sector officials. Continuing to expeditiously and effectively address the integrity of the court system and of the related investigatory and enforcement authorities is a necessary precondition for the implementation of any credible improvements in the regulation and supervision of Nigerian securities markets.

22. **Nigeria has made a high-level political commitment to address its strategic AML/CFT deficiencies.** However, according to the FATF, Nigeria has not made sufficient progress in implementing its action plan and certain deficiencies remain, including addressing issues regarding criminalization of money laundering and terrorist financing.

## VI. MAIN FINDINGS

23. **Principles relating to the regulator.** The SEC has a clear mandate imbedded in the ISA. The ISA does not guarantee full independence of the SEC. The SEC is a member of the FSRCC. Its powers and authorities are sufficient. Certain core regulatory competencies do not appear to be well represented among the current SEC staff, despite the fact that its manpower overall seems ample vis-à-vis the current size and level of development of the Nigerian securities market. Even though increased over the past few years, the proportion of staff engaged in the core regulatory and supervisory functions is still only 30 percent. The SEC is authorized to issue rules and regulations subject to public consultation. The public consultation process is not well defined and allows for a significant amount of SEC discretion.

24. **Principle relating to self-regulation.** The Nigerian regulatory system makes use of self-regulatory organizations (SRO), but currently only the NSE acts as such. The process for assigning a body as an SRO and the regulatory requirements on other types of SROs than securities exchanges and capital trade points<sup>1</sup> are unclear.

25. **Principles relating to enforcement.** The SEC's discharge of its functions falls short of expectations, mainly in the areas of inspections, investigations and enforcement. The departments responsible for these functions are not communicating and coordinating adequately. The SEC has comprehensive enforcement powers. It has used them for administrative, civil and criminal actions, but work remains to be done to ensure their effective and consistent use. The decisions to take enforcement action are not always made in a timely manner. The SEC has now outsourced some of its enforcement cases to expedite the processes. However backlogs exist also at the level of the police and the EFCC.

26. **Principles relating to cooperation.** The SEC cooperates both at the domestic and international level with its counterparts and other authorities. It is a member of the FSRCC. The FSRCC members have signed an MoU. It is also member of the FRC established by the FRC Act 2011. The SEC is a signatory to the IOSCO MMoU, and as such it is in a position to fully assist foreign securities regulators and share information with them, even though the MMoU has so far been used only in a limited number of investigations.

27. **Principles relating to issuers.** The disclosure standards for the Nigerian securities markets are generally sound. The requirements for issuers were recently amended to include new disclosure obligations and to take into consideration the need for internal controls and risk management. The concrete value of the new disclosure requirements will be entirely predicated upon the quality of implementation of the accounting and auditing standards in Nigeria, which is still work in progress.

28. **Principles for auditors, credit rating agencies (CRAs) and other information service providers.** The approval of the FRC Act and the creation of the FRC as the sole regulator responsible for the issuance of accounting standards as well as monitoring and ensuring the accuracy, veracity and fairness of accounting and financial reports of public interest companies is an important improvement. The FRC has developed a roadmap for the adoption of IFRS in Nigeria in 2012. It has yet to start its oversight of companies, accountants and auditors' compliance with the accounting and auditing standards. Capital market consultants that provide analytical and evaluative services are subject to registration. There is no specific regulatory framework for sell-side analysts. CRAs that provide credit ratings for securities registered in Nigeria have to be either registered or exempted from registration by the SEC.

---

<sup>1</sup> Capital trade point is the ISA term for the non-exchange multilateral trading systems (see Principle 33).

29. **Principles relating to collective investment schemes and hedge funds.** All fund managers and collective investment schemes are required to be registered. Most schemes are unit trusts, and they are required to have a fund manager, trustee and custodian. The fund manager cannot be a related party of the trustee or custodian. The SEC conducts yearly on-site inspections on the schemes, where the focus is on compliance with the legal requirements. Initial disclosure requirements in a partially standardized format apply, but there are no requirements for ongoing and periodic disclosures. Requirements on valuation of CIS assets are in place, while there are no rules on disclosure of prices of fund units. The establishment of hedge funds or marketing of foreign hedge funds to Nigerian investors would require registration by the SEC; currently there are no hedge funds offered to Nigerian investors.

30. **Principles relating to market intermediaries.** Market intermediaries need to be registered as Capital Market Operators for the specific functions they provide. The licensing process currently focuses on assessing the fitness and propriety of a limited number of sponsored individuals. Controllers are not assessed by the SEC, and the pre-registration inspection and registration committee meeting do not include a comprehensive assessment of the company applying for registration. Initial capital requirements are very low, and they are not adjusted for risk on an ongoing basis. Monitoring of compliance with the capital requirements and early intervention powers of the SEC are not adequate. Most conduct of business requirements are in place, but there are limited organizational requirements. The SEC inspects market intermediaries only for cause, and the amount of inspections has been very low at least during the past three years. The SEC has extensive powers to deal with an intermediary failure, but there is no plan on their use.

31. **Principles relating to secondary markets.** Securities exchanges and capital trade points are subject to registration. There are very limited requirements on technology, order execution procedures and equitable access to the trading systems. The enforcement action taken by the SEC in 2010 against the previous management of the NSE relating to its persistent governance problems brought the exchange under the SEC's close monitoring; the situation is normalizing after the appointment of the new CEO. Both the SEC and the NSE conduct market surveillance, but have not been effective in detecting, investigating and prosecuting market abuse, even though certain improvements have recently been achieved. There are no regulatory requirements for pre- and post-trade transparency. While the securities settlement system effectively addresses the risk of non-delivery of shares, there are no limits for the value of the cash settlement obligations of broker-dealers.

**Table 1. Nigeria: Summary Implementation of the IOSCO Principles—Detailed Assessments**

| <b>Principle</b>   | <b>Grade</b> | <b>Findings</b>   |
|--|--------------|---|
| Principle 1. The responsibilities of the Regulator should be clear and objectively stated.   | FI           | The SEC has a clear mandate derived from the ISA. It is a member of the FSRCC and has signed a multilateral MoU which includes other relevant domestic financial regulators.  |
| Principle 2. The Regulator should be operationally independent and accountable in the exercise of its functions and powers.                    | PI           | The ISA does not provide the SEC with full independence. The minister of finance has the power to give directives to the SEC, modify or rescind the rules proposed by the SEC, and exempt certain persons from the application of the ISA after consultation with the SEC. The last power has been used once. The possible need for the SEC to repatriate funds to the Federal Ministry of Finance (FMF) has the potential of undermining the SEC's independence in case of continued operating deficits. Currently, eight of the nine positions of the SEC Board are vacant, with the Director-General as the only Board member. Internally the SEC is functioning with Acting Commissioners.<br><br>The SEC Board members and staff have legal protection for acts done in good faith. Certain accountability mechanisms are in place, including the requirement to publish an annual report, however overall such mechanisms are not robust. The consultation process is mandated by the ISA, but there is no formal procedure on how to conduct it. |
| Principle 3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.    | BI           | The SEC has adequate powers; however they do not appear to be used effectively. It does not have sufficient policies and governance practices to perform its functions efficiently and effectively. The SEC is self-funded through fees and penalties levied from regulated entities. Market participants do not perceive the SEC as an attractive place to work for the most talented. The overall level of technical expertise in the key functions of the SEC is less than optimal. Its technology infrastructure appears to be insufficient to maintain efficient processes and support its statutory functions.  |
| Principle 4. The Regulator should adopt clear and consistent regulatory processes.   | PI           | The ISA contains consultation requirements and the SEC consults regularly with market participants; however the consultation process is not well established. Information about certain processes can be accessed via the SEC's web page. Some enforcement sanctions are disclosed. The IST is in charge of providing redress to individuals affected by the SEC's decisions. The SEC is generally required to provide reasons in writing for its decisions. Judicial redress is available.   |
| Principle 5. The staff of the Regulator should observe the highest professional standards, including appropriate standards of confidentiality. | PI           | There is a Code of Ethics for SEC employees. The Code includes provisions for disclosure of personal securities transactions to the SEC, confidentiality  |

| Principle   | Grade | Findings   |
|---|-------|--|
|   |       | obligations and sanctions for non-compliance. There are certain cooling-off period provisions in place. However, the Code does not appear to be implemented and enforced in practice. In 2009 the FSRCC initiated discussions on a comprehensive Code of Conduct for financial regulators. The draft Code includes more comprehensive conflict of interest provisions, and prohibitions on ownership and dealing with securities of regulated entities. There is no clear indication when or if the Code will be approved.                                     |
| Principle 6. The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.  | PI    | The SEC has not established any specific processes for the identification of systemic risk. The FSRCC has set up a sub-committee on financial sector soundness, which has the objective of providing surveillance over potential risks emanating from various sub-sectors of the financial sector. The work is not yet very advanced. The SEC is planning to introduce a risk-based supervisory model, with systemic risk as one element to consider.  |
| Principle 7. The Regulator should have or contribute to a process to review the perimeter of regulation regularly.  | BI    | Even though the SEC does not have a distinct process to address the perimeter of regulation, it has sought to respond to the emerging regulatory needs. It has referred providers of illegal services possibly falling outside the regulatory perimeter to the criminal authorities. However the internal processes are not optimally set up. Since its mandate includes supervisory coordination, the FSRCC and its subcommittees discuss issues related to the perimeter of regulation. Recently these discussions have focused on consolidated supervision. |
| Principle 8. The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.   | BI    | The ISA and the SEC Rules and Regulations impose requirements for the management of conflicts of interest in various manners. For some regulated entities, this is addressed only through specific trading rules applicable to employees. Prohibitions and disclosure obligations address misalignment of incentives of issuers. The monitoring of such obligations by the SEC is not robust.  |
| Principle 9. Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities. | PI    | Even though the Nigerian regulatory system makes use of self-regulatory organizations, the process for assigning a body as an SRO and the regulatory requirements on other types of SROs than securities exchanges and capital trade points are unclear. The SROs are required to inform the SEC of the disciplinary measures they have taken, and the SEC is not precluded from carrying out inspections of dealing members. In practice the SEC and NSE appear to coordinate and cooperate in their supervisory activities only to a limited extent.         |
| Principle 10. The Regulator should have comprehensive inspection, investigation and surveillance powers.  | FI    | The SEC has comprehensive powers to request information from and conduct inspections in regulated entities. It has been assigned the power to conduct market surveillance.   |

| Principle  | Grade | Findings  |
|--|-------|---|
| Principle 11. The Regulator should have comprehensive enforcement powers.  | FI    | The SEC has ample powers to request information from regulated entities and third parties. In the case of bank records the SEC relies in practice on the assistance of the CBN. The SEC enforcement tools include fines, bans, and suspension and revocation of registration.   |
| Principle 12. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program. | PI    | The regulatory system contains tools for inspection, investigation, surveillance and enforcement. On-site inspections are used mainly in relation to the issuance of new securities, and to verify compliance with the requirements relating to CIS. The SEC has comprehensive enforcement powers, but work remains to be done to ensure their effective and consistent use. In practice enforcement tools are primarily used to tackle minor issues, mostly delays in filing mandatory reports, rather than major violations of securities law and rules. However, the SEC has worked to improve its enforcement capabilities, including by obtaining assistance from a foreign regulator. It has also tried to address its own capacity problems by outsourcing several enforcement cases to law and audit firms. |
| Principle 13. The Regulator should have authority to share both public and non-public information with domestic and foreign counterparts.  | FI    | The SEC has the power conferred by the ISA to enter into cooperative agreements with domestic and foreign regulators. This broad power includes the power to share information.   |
| Principle 14. Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts.  | BI    | The SEC has signed an MoU at the FSRCC level for domestic information sharing among the relevant financial regulators. Cooperation among financial regulators through the FSRCC was reactivated after the crisis. The SEC is a signatory to the IOSCO MMoU. The SEC informed that it has received requests for specific investigatory assistance via the IOSCO MMoU, but information on the total number of requests was not readily available during the mission.  |
| Principle 15. The regulatory system should allow for assistance to be provided to foreign Regulators who need to make inquiries in the discharge of their functions and exercise of their powers.        | FI    | The regulatory system allows the SEC to provide assistance to foreign regulators. The SEC collects information on behalf of foreign regulators.   |
| Principle 16. There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions.  | FI    | Issuers of public offers are required to submit a prospectus for approval by the SEC. There are periodic and ongoing disclosure requirements applicable to issuers, with the latter arising from the NSE rules. Monitoring of issuers' compliance with their reporting obligations tends to concentrate on administrative aspects rather than fundamental issues, such as monitoring trading disclosures by company insiders. Cross-border offerings are contemplated in the ISA; however they are almost non-existent in practice.   |
| Principle 17. Holders of securities in a company should be treated in a fair and equitable manner.   | PI    | The CAMA contains the shareholders' fundamental rights, and the ISA includes additional protections   |

| Principle   | Grade | Findings  |
|---|-------|---|
|   |       | through more stringent disclosure requirements. Tender offers are regulated, but rare with only one in the last five years. The legal requirements for the disclosure of major shareholdings are fairly appropriate, but in practice the investors do not have sufficient access to the disclosures since they are not electronically available. The new SEC Corporate Governance Code, while of a voluntary nature, introduces new provisions aligned with best practices and international standards. |
| Principle 18. Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality.  | BI    | For the financial year starting in January 2012 issuers must submit, simultaneously to the SEC and the NSE, their financial statements according to the International Financial Reporting Standards (IFRS). The FRC is responsible for enforcing compliance with the IFRS. However, it has not yet fully established itself as the enforcer of accounting standards due to its recent establishment.  |
| Principle 19. Auditors should be subject to adequate levels of oversight.   | PI    | With the enactment of the FRC Act in 2011 and the commencing of the FRC's operations as the new auditor regulator, a significant change is expected in the auditor oversight. However due to its recent establishment, its oversight functions are not yet fully operational.   |
| Principle 20. Auditors should be independent of the issuing entity that they audit.   | PI    | Auditor independence is required in legislation; however the monitoring has in the past fallen short of international standards. The FRC is currently establishing its processes to monitor auditor independence.   |
| Principle 21. Audit standards should be of a high and internationally acceptable quality.   | BI    | Audits of the financial statements presented to the SEC must be conducted using International Standards on Auditing. The FRC is now responsible for promoting the highest standards among auditors and improving the quality of audit services.   |
| Principle 22. Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision. | PI    | Credit ratings are used for various regulatory purposes in Nigeria, and credit rating agencies are subject to a requirement to register with the SEC or, in the case of foreign CRAs, be exempted from registration. They are required to submit periodic reports to the SEC. The SEC has not yet conducted any on-site inspections of CRAs. The IOSCO Code of Conduct Fundamentals for CRAs has not yet been implemented, and only some of its elements are in place through other regulatory means.   |

| Principle   | Grade | Findings   |
|---|-------|--|
| Principle 23. Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.          | PI    | Independent sell-side analysts would be regulated as investment advisors, but no such firms currently exist. Those that provide analytical services ancillary to their other activities are subject to the requirements applicable to market intermediaries. Deficiencies exist in the requirements for the management and disclosure of conflicts of interest and related requirements for firms' internal procedures and controls.   |
| Principle 24. The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a collective investment scheme.   | BI    | All CIS and their fund managers, trustees and custodians are required to be registered. The registration requirement also applies to those that market a CIS. The most important organizational requirements are in place, whereas there are gaps in conduct of business rules. Fund managers and their trustees and custodians are subject to an extensive on-site inspection program, but the recent inspections have not covered the financial capacity of the fund manager and other prudential requirements. Fund managers are required to file comprehensive periodic reports with the SEC.  |
| Principle 25. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.   | FI    | Most CIS in Nigeria have adopted the legal form of investment trust, even though other forms are also possible. The current requirements for the segregation and protection of client assets are comprehensive. The SEC has extensive powers to take various enforcement measures, including winding up of a CIS or a fund manager.  |
| Principle 26. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme. | BI    | A potential investor in a CIS needs to be provided with a prospectus registered with the SEC, whose content is subject to minimum requirements. Together with the trust deed, it provides fairly comprehensive information on the CIS, its manager, trustee and custodian. There are no explicit requirements on periodic reporting to investors. The advertisements are subject to the approval of the SEC.   |
| Principle 27. Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.  | BI    | The regulatory framework requires CIS assets to be valued at fair market price, and the SEC has specified additional requirements for unlisted securities. The auditor of a CIS is required to certify that the scheme has been operated according to the regulatory requirements. The trust deed needs to address the subscription and redemption rights of unit holders, and the manner of calculating the subscription and redemption prices is regulated by the SEC. The industry has developed recommendations on the disclosure of unit prices and the provision of periodic information to investors. The treatment of pricing errors is not addressed in the regulatory framework. |
| Principle 28. Regulation should ensure that hedge funds and/or hedge funds managers/advisers are  | NA    | There are currently no hedge funds in Nigeria and the SEC Rules and Regulations would need to be   |

| Principle   | Grade | Findings  |
|---|-------|---|
| subject to appropriate oversight.   |       | amended to allow the establishment of hedge funds. Marketing of a foreign hedge fund to Nigerian investors would also require amendments to the Nigerian regulatory framework.  |
| Principle 29. Regulation should provide for minimum entry standards for market intermediaries.  | PI    | The regulatory framework requires market intermediaries to be registered by the SEC, and the minimum requirements for registration are clearly defined. The registration process focuses on the 3–4 sponsored individuals (as selected by the applicant) for each company applying for registration, instead of subjecting all directors to a full fitness and propriety assessment. Shareholders and other parties in a position to exercise control over the applicant are not evaluated by the SEC. The pre-registration inspection focuses on assessing the facilities of the applicant, and the Registration Committee meeting does not appear to sufficiently scrutinize the applicants. The SEC can cancel registration only as an enforcement measure, which seems to have contributed to the continued existence of many inactive companies. |
| Principle 30. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.   | NI    | The initial capital requirements of market intermediaries are very low, and ongoing capital requirements are not risk-based. The record-keeping and reporting requirements are not sufficient to determine and monitor the development of the capital level of market intermediaries on an ongoing basis. The SEC’s possibility to intervene in case of deteriorating capital is limited to failures, insolvency and other “grave” situations, and it is not clear whether it has exercised its powers effectively in such situations. The Nigerian prudential framework for market intermediaries does not currently address risks from outside the intermediary.  |
| Principle 31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters. | PI    | The most important conduct of business rules are in place in Nigeria, but the legislative and regulatory framework covers organizational requirements, including responsibility of the management, internal controls, risk management and management of conflicts of interest only in a limited manner. At least during the past three years, the SEC has conducted only for cause inspections of market intermediaries. Its inspection program is complemented by inspections conducted by the NSE (see Principles 9 and 34).  |
| Principle 32. There should be procedures for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.  | PI    | The SEC has extensive powers to act in the case of a failure of an intermediary, but no examples were available on the use of those powers. Its early warning system is based on quarterly returns, and it does not have a plan for dealing with an intermediary failure. The investor protection fund of the NSE required by law is not yet operational, and the SEC is in the process of establishing the nationwide trust scheme that it is required to maintain under the ISA.  |

| Principle  | Grade | Findings   |
|--|-------|--|
| Principle 33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.   | PI    | The requirements for registration as a securities exchange or capital trade point are set out in the ISA. The SEC lacks supervisory expertise in the area of exchange supervision. This combined with the lack of legal clarity on the distinction between various types of trading systems is a source of concern, given the exchanges' role as a key market infrastructure. The regulatory requirements on trading rules and order execution procedures are very limited.  |
| Principle 34. There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants. | BI    | Since 2009, the supervision of the NSE has been subject to extraordinary circumstances that culminated to the enforcement measures undertaken by the SEC in August 2010. This has led to a situation where an on-site inspection has not been considered necessary. The quarterly reporting from the exchange has continued in the normal manner. Both the SEC and NSE conduct market surveillance and supervise broker-dealers. The NSE has suspended a significant number of dealing members in 2011 and 2012, but mostly for reporting delays.  |
| Principle 35. Regulation should promote transparency of trading.   | NI    | The regulatory framework or the NSE rules do not specify any pre- and post-trade transparency requirements or objectives. The conditions for derogations from pre-trade transparency and waivers from post-trade transparency are not defined in the regulatory framework or NSE rules.  |
| Principle 36. Regulation should be designed to detect and deter manipulation and other unfair trading practices.   | PI    | The regulatory framework prohibiting market abuse is in place in Nigeria. However, the surveillance and enforcement activities conducted by the SEC and NSE do not appear to be effective in tackling market abuse, even though certain improvements have recently been achieved (see also Principle 12).  |
| Principle 37. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.  | PI    | The settlement system operated by the CSCS does not have any particular mechanisms in place to manage the risks arising from the payment obligations relating to the transactions made, beyond relying on the ability of dealing members and ultimately settlement banks to settle the cash leg, where necessary, or resorting to the trade guarantee fund in case of default. The NSE introduced short selling in September 2012 and the arrangements adopted currently appear to address the risks arising from short selling. However, there are no reporting requirements to the market or to the regulator. |
| Principle 38. Securities settlement systems and central counterparties should be subject to regulatory and supervisory requirements that are designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.  | NA    | Not assessed.  |
| <b>Fully Implemented (FI), Broadly Implemented (BI), Partly Implemented (PI), Not Implemented (NI), Not Applicable (NA)</b>  |       |  |

## VII. RECOMMENDED ACTION PLAN AND AUTHORITIES' RESPONSE

### A. Recommended Action Plan

**Table 2. Nigeria: Recommended Action Plan to Improve Implementation of the IOSCO Principles**

| <b>Principle</b> | <b>Recommended Action</b>   |
|------------------|---|
| Principle 2      | <ol style="list-style-type: none"> <li>1) The government should expeditiously appoint the SEC Board members.</li> <li>2) Going forward, the government should consider staggered terms for the members of the SEC Board.</li> <li>3) The government should strengthen the independence of the SEC by eliminating (a) the need for the ministerial approval for the SEC Rules and Regulations; (b) the power of the minister of finance to issue directives to the SEC; and (c) the power of the minister of finance to exempt individuals from the application of the ISA.</li> </ol> |
| Principle 3      | <ol style="list-style-type: none"> <li>1) The SEC should establish policies and governance practices to perform its functions efficiently and effectively.</li> <li>2) The SEC should continue to increase the proportion of staff engaged in the core regulatory and supervisory functions.</li> <li>3) The SEC should adopt adequate mechanisms to attract talented and skilled staff.</li> </ol>   |
| Principle 4      | <ol style="list-style-type: none"> <li>1) The SEC should ensure that its powers and discharge of its functions are consistently applied.</li> <li>2) The SEC should establish written procedures for its key functions, including rule-making and consultation to ensure due and efficient process.</li> <li>3) The SEC should consider publishing the comments received to rule consultations.</li> </ol>  |
| Principle 5      | <ol style="list-style-type: none"> <li>1) The SEC should strengthen transparency of and compliance with its Code of Ethics and Code of Conduct.</li> <li>2) The FSRCC should approve the Code of Conduct for Financial Regulators.</li> </ol>   |
| Principle 6      | The SEC should strengthen its expertise in analyzing the potential systemic risks arising from securities markets.  |
| Principle 7      | The SEC should consider adopting a systematic process for the review of the perimeter of regulation.  |
| Principle 8      | The SEC should introduce an overarching requirement for the avoidance, management and disclosure of conflicts of interest applicable to regulated entities.   |
| Principle 9      | <ol style="list-style-type: none"> <li>1) The SEC should make a strategic decision on the role of various types of SROs in the regulation and supervision of Nigerian securities markets, and based on that, clearly define the SROs' responsibilities in the regulatory framework.</li> <li>2) The SEC and NSE should intensify their cooperation and coordination in market surveillance, member supervision and supervision of listed companies.</li> </ol>  |
| Principle 12     | <ol style="list-style-type: none"> <li>1) The SEC should review and expand the coverage of its on-site inspection program.</li> <li>2) The SEC should improve coordination between the departments in charge of registration, monitoring, inspections, investigations and enforcement.</li> <li>3) The SEC should re-deploy resources to address the more serious securities violations, such as market manipulation and insider trading.</li> </ol>  |
| Principle 14     | The SEC should ensure that its procedures for providing assistance to foreign regulators are well coordinated and documented.   |

| Principle        | Recommended Action   |
|------------------|--|
| Principle 17     | <ol style="list-style-type: none"> <li>1) The SEC should, in cooperation with the NSE, improve investors' access to the information on changes in major shareholdings.</li> <li>2) The SEC should establish effective mechanisms to conduct on-going monitoring of trading by company insiders.</li> </ol>   |
| Principles 18-21 | <ol style="list-style-type: none"> <li>1) The government should appoint the FRC Board.</li> <li>2) The SEC and FRC should collaborate in monitoring issuers' IFRS compliance.</li> <li>3) The SEC should develop its technical expertise in IFRS.</li> <li>4) The FRC should conduct inspections to monitor auditor independence.</li> </ol>   |
| Principle 22     | <ol style="list-style-type: none"> <li>1) The SEC should introduce an on-site inspection program for CRAs.</li> <li>2) The SEC should implement the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies.</li> </ol>  |
| Principle 23     | The SEC should ensure that the conflict of interest rules that need to be implemented for all Capital Market Operators sufficiently address the conflicts of interest inherent in the work of sell-side analysts.  |
| Principle 24     | The SEC should introduce additional conduct of business requirements for fund managers to ensure fair treatment of clients.  |
| Principle 26     | The SEC should develop ongoing and periodic disclosure requirements for fund managers, in coordination with the industry initiatives.  |
| Principle 27     | The SEC should ensure that the regulatory framework includes sufficient requirements to ensure availability of up-to-date price information to investors and to deal with any pricing errors in a fair and equal manner.   |
| Principle 29     | <ol style="list-style-type: none"> <li>1) The SEC should amend the regulatory framework to ensure that all directors, significant shareholders and all those in a position to exercise control over a market intermediary are subject to a sufficient fitness and propriety assessment.</li> <li>2) The SEC should pay more attention in its pre-registration inspection to internal organization, risk management and supervisory systems.</li> <li>3) The SEC should address the high number of inactive Capital Market Operators by facilitating the easier cancellation of registrations.</li> </ol> |
| Principle 30     | <p>The SEC should expeditiously revise the capital requirements of market intermediaries by:</p> <ol style="list-style-type: none"> <li>1) introducing higher initial capital requirements and ongoing risk-based capital requirements;</li> <li>2) strengthening the ongoing monitoring of capital levels;</li> <li>3) facilitating prompt corrective action in case of deteriorating capital levels; and</li> <li>4) using its existing enforcement tools more effectively to require recapitalization of undercapitalized market intermediaries.</li> </ol>   |
| Principle 31     | <ol style="list-style-type: none"> <li>1) The SEC should introduce requirements addressing the responsibility of the management and various organizational requirements for market intermediaries.</li> <li>2) The SEC should complement, or where appropriate replace, the current product-related on-site inspections with entity-based inspections.</li> </ol>  |
| Principle 32     | <ol style="list-style-type: none"> <li>1) The SEC, preferably in cooperation with the other members of the FSRCC, should formalize a written plan for dealing with an intermediary failure.</li> <li>2) The SEC should try to expeditiously address the current lack of an investor compensation regime in Nigeria.</li> </ol>   |

| Principle    | Recommended Action  |
|--------------|---|
| Principle 33 | <ol style="list-style-type: none"> <li>1) The SEC should increase its expertise in the supervision of exchanges and other trading platforms.</li> <li>2) The SEC should enhance the operational requirements applicable to trading platforms.</li> <li>3) The SEC should ensure that the regulatory requirements for various types of trading platforms are clearly and transparently set out in the regulatory framework.</li> </ol> |
| Principle 34 | <ol style="list-style-type: none"> <li>1) The SEC should establish an ongoing supervisory program for the NSE, addressing various aspects of its role as an operator of a key market infrastructure and as an SRO.</li> <li>2) The SEC should ensure that the NSE widens the use of the disciplinary measures available to it beyond suspensions in more serious cases.</li> </ol>  |
| Principle 35 | The SEC should introduce minimum regulatory requirements on pre- and post-trade transparency, with clear conditions on exemptions and delays.   |
| Principle 36 | The SEC should continue to address its current lack of effectiveness in fighting market abuse, and ensure that the NSE also complies with its obligation to refer cases to the SEC.   |
| Principle 37 | The SEC should ensure that the CSCS settlement system sufficiently deals with the risk that failed settlement of large transactions can cause to the financial system.  |

### **B. Authorities' Response to the Assessment**

32. We sincerely appreciate the opportunity to provide our written comments on the assessors' report and express our gratitude to the assessors for the scope of their assessment. We welcome the assessment, given our commitment to ensuring best practice regulation and world class capital markets. We agree broadly with most of the recommendations on improving the Nigerian capital market infrastructure and strengthening regulation. We however express strong reservations on many of the observations contained in the report, some of which were not discussed with us by the team during their mission. The assessors in their report concede that 'it was not possible for them to discuss with a sufficient pool of market participants or public sector authorities with tasks relating to securities markets'. This may well have contributed to certain observations and conclusions that do not reflect the current circumstances in the Nigerian capital market. In addition to the acknowledgement of the adequacy of the Investment and Securities Act of 2007, we expected the report to sufficiently highlight the widely acknowledged remarkable improvement in regulatory systems and processes in the Nigerian capital market, since the last assessment in 2002 and 10 years ago and most especially given the results of the proactive and bold reforms that the Commission embarked upon after the recent global financial crisis. Specific comments are presented below

33. The report makes an unfounded reference to the SEC not being free of corruption. We are shocked by this assertion given that the Director General, Ms. Arunma Oteh, has promoted and enforced the highest ethical standards within the SEC and in the Nigerian capital markets, since she assumed office in January 2010. The SEC's zero tolerance stance against corruption and market abuse has equally been widely acknowledged domestically and

internationally, encouraging the active participation of international investors (who make up about 70 percent of daily buy side trading by value on the Nigerian Stock Exchange) in the Nigerian capital markets. This allegation is without basis, and was not mentioned to us by the assessors during their mission. For such a serious allegation, albeit unfounded, we would have expected the assessors to provide specifics verbally or in writing, that will enable us investigate and ensure that the efforts of the Commission to become a role model in securities regulation are not undermined. When we learnt of this allegation through a draft of the assessors' report, we promptly reacted as follows: "It has been widely reported that the Director General of the Securities and Exchange Commission, since her assumption of duty in January 2010, has taken unprecedented steps to eliminate market abuse and corruption from the Nigerian capital market. She has not relented in the drive to root out corrupt practices despite push back from vested interests. These issues are widely reported [in the local and international media]. She took action to strengthen internal controls within the SEC, and has taken steps to initiate a whistle blowing policy." Steps are also being taken to establish an Ethics function and recruit an Ethics officer. We are extremely disappointed to note that while the final version of the report acknowledges the zero tolerance stance of the Director General against corruption, it still retains the weighty and unproven allegation against the Commission.

34. The SEC's Board was reconstituted in December 2012. During their mission in September 2012, the assessors observed that the SEC's Board had not been reconstituted since June 2012 when the tenure of most of the previous Board members expired. It is important to note that the minister of finance provides oversight in the absence of a Board which arose this time because of the rigorous process for the appointment of Board members including the confirmation by the Senate following the appointment by the president on the basis of the recommendation of the minister of finance.

35. The report erroneously states that the SEC is not considered an attractive employer. This assertion is contrary to empirical evidence and does not take account of the growing interest of seasoned professionals in Nigeria's public service. Our most recent recruitment process led to the appointment of 50 excellent candidates from a pool of 34,000 eminently qualified accountants, economists, lawyers and information technology and finance professionals attracted to the SEC. The Commission is also known to attract highly qualified professionals including graduates of Ivy League institutions such as Harvard University, and University of Pennsylvania, New York-admitted attorneys, U.K. qualified chartered accountants, chartered financial analysts and lawyers from top law firms, internationally. We continue to experience the same trend in the ongoing recruitment exercise. We nonetheless recognize that we need to continue to strengthen capacity by increasing the proportion of staff in the core mandate areas of the Commission. On enforcement, we have since taken steps to receive technical assistance from a major international counterpart. The recommendations made were generated jointly with SEC staff and cover delegation of authority, streamlining and strengthening of inspections, investigation and enforcement

structures as well as a revamped enforcement manual which when approved by the Board of SEC will make the Commission's enforcement regime, even more effective and efficient.

36. We also do not agree with the assessment on the inadequacy of broker dealer regulation and minimum capital requirements. While the SEC is in the process of fully implementing risk-based supervision, our existing rules and supervision framework have been sufficient to check abuse, and to limit any damage that may result from the failure of any operator. New policies, regulations and rules have been put in place since the global financial crisis to prevent excessive risk taking such as margin lending without adequate skills and systems to monitor and manage positions. For example, the Nigerian SEC and the CBN jointly issued margin lending guidelines in 2010 amongst other rule changes following the global financial crisis. Mandatory provisions relating to capital requirements have also been closely monitored and enforced. It is important to note that the minimum capital requirements in Nigeria are higher than in a number of jurisdictions including some developed markets. In 2012, we established a Committee that comprised representatives of broker/dealers, the Nigerian Stock Exchange and the Commission to review the existing capital requirements and propose new guidelines, along with fit and proper guidelines for brokers. These guidelines will be presented to the Board of SEC for consideration. Far from the impression created by the report, onsite supervision in 2011 was only suspended in a bid to restructure our inspection mechanisms. It is therefore inappropriate to say we rarely inspect broker dealers. Staff carried out offsite inspections including rigorous reviews of periodic returns, both monthly and quarterly in 2011 and resumed onsite inspections in 2012.

37. The assessment appears to understate the rigour and success of our enforcement efforts. The report suggests erroneously that we have only focused on administrative penalties while since January 2010, we have taken very widely publicized enforcement action against the then leadership of the Nigerian Stock Exchange, and instituted legal proceedings against 260 individuals and entities for various forms of market infractions including insider dealing, share price manipulation and market abuses. As testimony to the quality of our investigations, we have begun to receive favorable court orders for disgorgement of illegally gained profits. Since 2010, we have established effective partnerships with the Attorney General's office, and the Nigeria Police, both of whom have resident officers within the Commission. This has strengthened the Commission's enforcement activities, and made us more effective and efficient including expediting the process of shutting down pyramid schemes and other such fraudulent devices.

38. In certain instances, the assessors did not appear willing to take note of information we provided, which negated their prior assessments. A good example is the SEC's relationship with regulators from other jurisdictions which are governed by bilateral and multilateral memoranda of understanding (MoU's). The assessors specifically claimed that the MOUs were used in a limited manner. We do not understand this claim since all requests made were treated adequately and in many cases were made by highly regarded regulators, and in connection with very important, well-publicized cross border investigations. We do

not measure success by the number of requests since it is not our place to solicit them. On a related note, we regret that the assessors do not share our view that the contents of bilateral MoU's do not necessarily have to be published on our website since they are bilateral agreements. We have instead published a list of national regulators with whom we have outstanding MoU's.

39. Though the assessors acknowledge the robustness of investor protection provisions in Nigerian law, they have understated the equally robust disclosure regime. Specifically, we further strengthened our disclosure regime in 2011 by introducing a number of new measures including the introduction of a revised code of corporate governance which requires listed companies to indicate, the extent of compliance with the code, in their annual reports. Nigeria is recognized in indices such as the World Economic Forum's Global Competitiveness Index and the World Bank's Doing Business Report as a leading country for investor protection.

40. We do not understand why the assessors have ignored the robust provisions of our enabling law and in particular Rule 20A, which mandate operators to inform the Commission and to publish in dailies, when they are discontinuing business. It is surprising that contrary to this clear evidence, the assessment retains the claim that such operators are not required to inform us of their discontinuance of any business activity registered with the Commission

41. Another area not acknowledged in the report is the adoption of International Financial Reporting Standards (IFRS), effective 2012. In 2010, the Federal Executive Council, chaired by the President of Nigeria, considered and approved a roadmap in 2010 on the adoption of IFRS prepared by a Committee of industry experts and regulators including SEC. The roadmap articulated a calendar for migration to IFRS including 2012 for listed companies and 2013 for capital market operators. As part of our market development efforts we have since 2010 actively supported the IFRS migration process. Indeed, we received funding support from the World Bank to engage the services of the Institute of Chartered Accountants of England and Wales, and engaged the services of one of the international accounting firms, to assist us with this important initiative.

42. It is also erroneous to retain in the report as the assessors have done, a statement to the effect that we cancel registration of capital market operators only as an enforcement measure. We actively monitor the status of registered entities, and we withdraw registration in justifiable cases. In fact, we recently cancelled the registration for 35 operators, not as an enforcement measure.

43. Contrary to the assessment report, the Commission has a robust consultation process for rule-making. We provided these details and are surprised that our comments are not adequately reflected in the report. Rule-making is an important element of the Nigeria SEC regulatory framework. Rules originate from proposals made by staff, market participants and other stakeholders and are developed and drafted by relevant divisions of the SEC. They are

then considered by the Rules Committee (comprising directors in various critical departments) and exposed to the market, via correspondence with the Trade Groups, publication in the national dailies and the SEC website. The comments received from stakeholders are also sometimes discussed at the industry wide capital markets committee meetings. Feedback from the market is collated and used in the final review of the draft Rules and are presented to the Board of the Commission for consideration alongside the draft Rules. The approved rules are then presented to the minister for ratification. Section 313 of the Investment and Securities Act specifically requires that the SEC consult in this manner. We therefore believe that we have a comprehensive and inclusive process that compares favorably with the highest standards, globally.

44. We have elaborate rules to deal with the failure of an intermediary, contrary to the assessment report. Sections 48 to 53 of the Investments and Securities Act are entirely dedicated to this matter. They provide elaborate powers to the Commission to resolve the failure or near failure of an intermediary in a manner that avoids contagion.

45. Oversight of the NSE. The nature of the presentation of the issues related to the NSE could give the erroneous impression that there has been insufficient oversight of the NSE. Following the September 2009 inspection of the NSE, the SEC started close monitoring of the NSE. This included bimonthly meetings at the Executive Management level and culminated in an intervention in August 2010. The intervention led to the removal of the leadership of the NSE due to corporate governance lapses and financial mismanagement. An interim team of seasoned professionals was appointed to stabilize the Exchange and oversee the recruitment of a new leadership team. That team made periodic reports, at least, quarterly to the Board of SEC. In addition, SEC appointed eight public interest members to the Council (the equivalent of a Board) of the NSE. Those council members completed their assignment during the 3<sup>rd</sup> quarter of 2012. The new leadership team that took over starting in April 2011 has taken significant steps to reposition the NSE as a world class exchange with best practice corporate governance practices and trading systems. As indicated in the assessors' report, the SEC through the various mechanisms described above has closely monitored the NSE. Normal annual inspections will resume in 2013.

46. We note that in a number of cases that the final grade assigned by the assessors did not reflect their written assessment or the current circumstances in the Nigerian capital markets. Examples include the assessment of the extent of compliance with principles 24, 26, and 27 with respect to collective investment schemes and Principle 34 with respect to exchanges and trading systems.

47. We appreciate the opportunity to provide the above comments and will be pleased to provide any clarification needed.

## VIII. DETAILED ASSESSMENT

48. **The purpose of the assessment is primarily to ascertain whether the legal and regulatory securities markets requirements of the country and the operations of the securities regulatory authorities in implementing and enforcing these requirements in practice meet the standards set out in the IOSCO Principles.** The assessment is to be a means of identifying potential gaps, inconsistencies, weaknesses and areas where further powers and/or better implementation of the existing framework may be necessary and used as a basis for establishing priorities for improvements to the current regulatory scheme.

49. **The assessment of the country's observance of each individual Principle is made by assigning to it one of the following assessment categories:** fully implemented, broadly implemented, partly implemented, not implemented and not applicable. The IOSCO assessment methodology provides a set of assessment criteria to be met in respect of each Principle to achieve the designated benchmarks. The methodology recognizes that the means of implementation may vary depending on the domestic context, structure, and stage of development of the country's capital market and acknowledges that regulatory authorities may implement the Principles in many different ways.

- A Principle is considered **fully implemented** when all assessment criteria specified for that Principle are generally met without any significant deficiencies.
- A Principle is considered **broadly implemented** when the exceptions to meeting the assessment criteria specified for that Principle are limited to those specified under the broadly implemented benchmark for that Principle and do not substantially affect the overall adequacy of the regulation that the Principle is intended to address.
- A Principle is considered **partly implemented** when the assessment criteria specified under the partly implemented benchmark for that Principle are generally met without any significant deficiencies.
- A Principle is considered **not implemented** when major shortcomings (as specified in the not implemented benchmark for that Principle) are found in adhering to the assessment criteria specified for that Principle.
- A Principle is considered **not applicable** when it does not apply because of the nature of the country's securities market and relevant structural, legal and institutional considerations.

**Table 3. Nigeria: Detailed Assessment of Implementation of the IOSCO Principles**

| <b>Principles Relating to the Regulator</b> |   |
|---|---|
| <b>Principle 1.</b>                         | The responsibilities of the regulator should be clear and objectively stated.   |
| Description                                 | <p><b>Regulation of the financial sector in Nigeria</b></p> <p>The financial sector in Nigeria is regulated and supervised by the following authorities:</p> <ul style="list-style-type: none"> <li>• The CBN – Licenses, regulates and supervises all commercial banks, savings and loans associations, and some non-banking financial institutions (including finance leasing);</li> <li>• The NAICOM – regulates and supervises insurance companies;</li> <li>• The National Pension Commission (PENCOM) - regulates and supervises pension funds;</li> <li>• Federal Ministry of Finance – sets overall financial and economic policies for Nigeria; and</li> <li>• The SEC, whose mandate and responsibilities are described below.</li> </ul> <p>In 2010 the CBN took the decision to repeal the universal banking regime. Banks in Nigeria were required to divest from all non-banking business, including the securities market activities they or their subsidiaries conducted. Today banks are not allowed to undertake non-banking activities, such as securities market activities, with the exception of being able to act as primary dealers or market makers subject to a registration by the Debt Management Office. The primary dealers can trade in debt securities for their own account and for the account of their customers in the over-the-counter (OTC) market. In addition, it is possible that the same holding company owns a bank and a Capital Market Operator, and some banks dealt with the CBN requirement by setting up a holding company structure.</p> <p><b>Mandate and responsibilities of the SEC</b></p> <p>The SEC is mandated to regulate and develop the Nigerian capital market. The responsibilities, powers and authority of the SEC are clearly and transparently stated in Section 13 of the Investments and Securities Act of 2007 (ISA). The powers and authority are enforceable. The ISA 2007 repealed the Investments and Securities Act 1999 and established the SEC as the apex regulatory authority for the Nigerian capital market to ensure the protection of investors, the maintenance of fair, efficient and transparent markets, and the reduction of systemic risk.</p> <p>The SEC market regulation mandate includes:</p> <ol style="list-style-type: none"> <li>1) <i>Registration</i> of securities and Capital Market Operators. Persons and instruments registered in the Nigerian market include: <ul style="list-style-type: none"> <li>• Securities and commodity exchanges and capital trade points</li> <li>• Futures, options and derivatives exchanges</li> <li>• Depository, clearing and settlement agencies</li> <li>• Capital Market Operators, including: <ul style="list-style-type: none"> <li>○ Issuing houses</li> <li>○ Securities dealers/stock brokers/sub-brokers</li> <li>○ Registrars/transfer agents</li> <li>○ Trustees</li> <li>○ Reporting accountants</li> <li>○ Solicitors</li> <li>○ Investment advisers</li> </ul> </li> <li>• Securities, including: <ul style="list-style-type: none"> <li>○ Equities</li> <li>○ Debentures</li> <li>○ Debt instruments</li> <li>○ Collective investment schemes.</li> </ul> </li> </ul> </li> <li>2) <i>Inspections</i> either done on-site or off-site.</li> <li>3) <i>Surveillance</i> carried out over exchanges and trading.</li> </ol> |

- 4) *Investigation* of alleged breaches of the laws and regulations governing the Nigerian capital market.
- 5) *Enforcement* actions taken against Capital Market Operators where needed after an investigation has been carried out. In minor cases, an all parties meeting is convened by the SEC where it mediates between parties involved in a dispute. In more serious cases or where no resolution is reached or a party fails to comply with a directive given at the all parties meeting, the defaulting party is called before the Administrative Proceedings Committee (APC), which is a quasi-judicial court, with only civil jurisdiction. Appeals against decisions of the APC are made at the Investments and Securities Tribunal (IST). Enforcement actions may be in the form of payment of a fine, a ban, a suspension, and a cancellation or revocation of registration. Criminal cases are forwarded to the Nigeria Police Force (NPF), Economic and Financial Crimes Commission (EFCC) or the Attorney-General of the Federation (AGF) where allegations are found to be criminal in nature.
- 6) *Rule-making* by the SEC as stated in Section 312(1)(o)-(p) of the ISA. The SEC may make rules and regulations for the purpose of giving effect to the provisions of the ISA, providing for anything requiring to be prescribed under the ISA and generally for carrying out the principles and objectives of the ISA. The SEC in the exercise of its rule making power consults with stakeholders. There are limitations to the SEC's rule making powers. The SEC Rules and Regulations to alter or modify the provisions of the Second Schedule of the ISA (Investment and Investment Business) require consultation with the minister of finance (Section 313(1)(a) ISA). Any SEC Rule or Regulation under the ISA will be deemed made fifteen days after receipt by the minister of finance, unless the minister of finance, before the expiration of the fifteen days, directs that it be modified, amended or rescinded (Section 313(4) ISA).

#### **Interpretation of authority**

There is no provision under the ISA that allows the SEC to interpret its authority.

The SEC has the authority to make rules and regulations for the purpose of giving effect to the provisions of the ISA, including in order to alter or modify the provisions of the Second Schedule of the ISA after consultation with the minister. The SEC in the exercise of its power to make rules must consult with stakeholders. The IST exercises jurisdiction to hear and determine any question of law of dispute involving a decision or determination of the SEC in the application of the ISA.

#### **Gaps or overlaps**

The responsibilities of the financial sector regulators are defined in acts designed to minimize the possibility of gaps or overlaps.

According to the ISA, in the Nigerian securities market there can be self-regulatory organizations (SROs) which include any registered securities exchange, capital trade point, association of securities dealers, clearing house, capital market trade association or any other self-regulatory body approved as such by the SEC. The SEC is required to promote and register SROs, to which it may delegate its powers.

As explained in Principle 9 the only SRO in Nigeria is currently the NSE. If there were capital trade points, they would also be considered SROs. The NSE has rules of eligibility for its members; according to the regulatory framework it establishes and enforces binding rules of trading and business conduct as well as establishes disciplinary rules and conducts disciplinary proceedings (see Principle 9).

#### **Coordination and cooperation between regulatory authorities**

After the adoption of the universal banking model, the SEC is solely in charge of the supervision of all securities market activities, including the limited activities that banks are entitled to undertake. As explained in Principle 13, the SEC is a member of the Financial Services Regulation Coordinating Committee (FSRCC). The FSRCC is an inter-agency body set up to deal with matters of common interest and concern to the various regulatory and supervisory authorities in

|                     |  |
|---------------------|--|
|                     | <p>the financial services industry. The FSRCC was created in 1998, but it adopted a more active role after the financial crisis that hit the Nigerian market in 2008.</p> <p>In 2009 the FSRCC started to produce new regulatory proposals on areas such as consolidated supervision of financial institutions. This has a potential impact also on the SEC if the consolidated supervision will be extended to groups of holding companies that include Capital Market Operators as subsidiaries (see also Principle 30). The arrangements for cooperation and communication between the authorities of the financial sector in Nigeria are in place, including appropriate channels of communication and certain level of cooperation. These have been established in a multilateral MoU signed by all domestic authorities.</p>   |
| Assessment          | Fully Implemented  |
| Comments            | <p>The SEC's powers and authority are clearly stated in the ISA and are enforceable (see Principle 12). There is no specific provision under the ISA that allows the SEC to interpret its authority. It is the IST that is authorized by law to interpret the ISA (Section 284(3) ISA).</p> <p>The communication and coordination between the SEC and the NSE is addressed in Principles 9 and 34, and that between the SEC and EFCC in Principle 12.</p>  |
| <b>Principle 2.</b> | The regulator should be operationally independent and accountable in the exercise of its functions and powers.   |
|                     | <p><b>Independence</b></p> <p>The SEC is a public law entity with its own legal personality and full public and private capacity.</p> <p><i>Governance</i></p> <p>The SEC's governing body is its Board (Section 3 ISA). The Board of the SEC includes nine persons:</p> <ul style="list-style-type: none"> <li>• a part-time chairman;</li> <li>• the director-general and chief executive as accounting officer;</li> <li>• three full time commissioners;</li> <li>• a representative of the federal ministry of finance;</li> <li>• a representative of the CBN; and</li> <li>• two part-time Commissioners one of whom is a legal practitioner qualified to practice in Nigeria with 10 years post call experience.</li> </ul> <p>The SEC has a four-member Executive Management Committee composed of:</p> <ul style="list-style-type: none"> <li>• the director-general; and</li> <li>• three executive commissioners in charge of Operations, Finance &amp; Administration, and Legal &amp; Enforcement.</li> </ul> <p>During the assessment mission, except for the Director-General, the rest of the Board positions were vacant. The three executive commissioner positions were filled by acting executive commissioners. That has been the situation since June 2012, when the term of the three full time SEC Commissioners, the chairman and the part-time commissioners appointed for a period of four years ended. The situation of ex-officio Commissioners is different due to the fact that according to the ISA they seem to have no established term (Section 5(2) ISA).</p> <p>The SEC workforce, as of the end of 2011, is composed of 630 members of staff spread across four directorates and seven zonal offices. The SEC has its headquarters at the Federal Capital Territory, Abuja, and operates through its seven zonal offices. The SEC is composed of seventeen departments. Seven of the seventeen departments are directly involved in regulation and supervision of markets.</p> <p>The Executive Commissioner, Operations, is responsible for the following departments:</p> |

- Securities and Investment Services (SIS): Registers and supervises the issuance of securities of public companies, as well as merger and acquisition activities. It is composed of 36 persons.
- Registration and Recognized Investment Exchanges (RRIE): Responsible for the registration of all Capital Market Operators and recognized securities exchanges. In addition, the department supervises the activities of securities exchanges and other trading platforms. It is composed of 32 persons.
- Collective Investment Schemes (CIS): Supervises unit trusts and venture capital activities. It is composed of 26 persons.
- Financial Standards and Corporate Governance (FS&CG): The department reviews the financial health of publicly quoted companies, and ensures compliance with the code of corporate governance and other relevant guidelines. It is composed of 21 persons.
- Research and Planning (R&P): Undertakes the market development functions of the SEC through research and other development activities. The department also serves as the Secretariat of both the monthly Executive Management Committee meeting and the Capital Market Committee (CMC), a quarterly interface with the market. It is composed of 52 persons.

The Executive Commissioner, Legal & Enforcement, is responsible for the following departments:

- Monitoring and Investigations (M&I): Monitors the financial health of Capital Market Operators to ensure that only fit and proper participants are in the market. It also investigates and resolves disputes among market stakeholders. It is composed of 34 persons.
- Enforcement & Compliance (E&C): Undertakes the enforcement and compliance functions of the SEC and serves as the secretariat of the APC. It is composed of 27 persons.

In addition, there is the Office of the Secretary to the Commission which serves as the Secretariat of the SEC's Board, its Committees and the Executive Management Committee. It offers advisory services to the Board on issues of compliance with applicable laws and regulations. It reports to the Director-General. It is composed of six persons.

The ISA contains mechanisms intended to protect the independence of the SEC which include procedures for appointment, terms of office and criteria for removal of the Board members. As a result, the Director-General and the three full time Commissioners are appointed by the President upon the recommendation of the minister of finance and confirmation by the Senate (Section 5(1) ISA).

The Board members' terms in office are established by the ISA. The Director-General holds office for a period of five years in the first instance and may be reappointed for a further period of five years and no more. The three full time Commissioners hold office in the first instance for a period of four years and may be re-appointed for a further term of four years and no more. The chairman and part-time commissioners (other than the ex-officio commissioners) each hold office for a term of four years and no more (Section 5(2) of the ISA).

The removal of the Board members must be for cause. A member of the Board ceases to hold office if he/she (Section 8 ISA):

- a) becomes of unsound mind;
- b) becomes bankrupt or makes a compromise with creditors;
- c) is convicted of a felony or any offence involving dishonesty;
- d) is guilty of serious misconduct in relation to his duties; or
- e) is a person who has a professional qualification, and is disqualified or suspended (other than at his/her own request) from practicing his/her profession in any part of Nigeria by the order of any competent authority.

The President may at any time, for one of the reasons indicated above, and upon the recommendation of the minister of finance remove the members of the Board. However, the removal of the full-time members of the Board of the SEC requires Senate's approval (Section 8 ISA).

The SEC's independence is impacted as the minister of finance, without prejudice to the provisions of the ISA, may give to the SEC directives as appear to him/her to be just and proper for the effective discharge of the SEC's functions. The SEC has the duty to comply. The power of the minister of finance seems not to exclude decision making on day-to-day technical matters. The assessors were informed that the minister of finance has never made use of the provision authorizing him/her to give the SEC a directive that it must comply with.

After consultation with the SEC, if the minister of finance is of the opinion that it is necessary or expedient to do so in the public interest, he/she may, by order published in the Gazette, exempt any person or class of persons buying or selling securities or otherwise dealing with the securities market from the operation of the provisions of the ISA (Sections 298, 309). The assessors were informed of a case where the minister of finance had used the ministerial prerogative under the ISA to exempt a person dealing with the securities market from the operation of some of the provisions of the ISA. The person was a public interest body. The exercise of this power to exempt by the minister of finance needs to be published in the Gazette (Section 309 ISA).

Every decision of the APC needs to be confirmed by the SEC Board before it becomes effective. The confirmation is to be made no later than thirty days after the decision was taken by the APC, provided that in the absence of the Board of the SEC, confirmation of the APC's decision is made by the minister of finance or any person performing that function (Rule 17: Decisions of the Committee as amended March 2010).

Mandatory consultation with the minister of finance by the SEC is required when the SEC intends to make rules and regulations to alter or modify the provisions of the Second Schedule of the ISA which deals with Investment and Investment Business (Section 313(1)(a) ISA). The consultation process is not established by law. Further, any SEC Rule or Regulation under the ISA will be deemed made fifteen days after receipt by the minister of finance, unless the minister of finance, before the expiration of the fifteen days, directs that it be modified, amended or rescinded (Section 313(4) ISA). Even though the Senate does not have any formal role in the operational decision making of the SEC, it appears that the SEC feels constrained in some of its decision making by the threat of an intervention on the part of the Senate. It was indicated that this perceived threat has also decreased the SEC's willingness to make proposals for legislative changes.

The APC is composed of non-executive SEC commissioners, directors of departments, and representatives from the ministry of finance and the CBN. Trade associations in the capital market participate in the APC but do not vote.

#### *The SEC funding*

The SEC establishes and maintains a fund into which the following is paid:

- (a) funds provided to the SEC by the federal government;
- (b) penalties, fees, charges and administrative costs of proceedings; and
- (c) monetary gifts, contributions and other funds that may be received by the SEC.

In practice the SEC is self-financed by fees imposed on regulated entities. The fees chargeable by the SEC in respect of all transactions with it are those as the SEC from time to time prescribes by notice published in two national newspapers (Rule 151). The Board of the SEC approves the SEC budget (Section 4 ISA). The Board submits every year to the minister of finance and the National Assembly an estimate of its income and expenditure (Section 26 ISA).

The SEC has a continuous source of funding sufficient to meet its regulatory and operational needs as long as the market is functioning well. If it is not the case, the SEC must use its accumulated fund. For example, in 2011 and 2010 the SEC had deficits. The deficits were covered by the SEC's accumulated fund. According to the SEC's audited financial statement, the accumulated fund had ₦23,471,808,000 (US\$148 million) in 2011. In 2010 the accumulated fund had ₦35,668,891,000.

As to the stability of the SEC's source of funding *The Report of the SEC Committee on the Nigerian Capital Market - Nigeria's capital market: Making world-class potential a reality, February*

2009, raised the issue of the requirement for the SEC to repatriate any excess funds to the Nigerian Treasury. The report considered necessary for the SEC to build reserves to fund the necessary expansion of its regulatory capacity. In August 2012 the Federal Ministry of Finance requested all the government agencies to remit their accumulated funds into the Consolidated Revenue Fund (CRF) Account. The SEC has been directed to remit the sum of ₦15 billion.

The SEC's operating expenses for 2011 were ₦9,092,486,000. Its income for 2011 was ₦6,895,403,000.

#### *Legal protection*

Officers, members and employees of the SEC are protected from suit, prosecution or other legal proceedings for anything which is done or intended to be done in good faith under the ISA or the SEC Rules and Regulations (Section 302 ISA). The assessors were informed that no suit, prosecution or legal proceeding has been initiated against SEC Board members or staff.

There is no provision that guarantees free legal defense for the SEC Board members and staff in connection with such type of actions brought against them.

#### **Accountability**

The SEC's Board prepares each year an estimate of the SEC's income and expenditure during the next succeeding year and submits it to the minister of finance and the National Assembly. The SEC must keep proper books and records and accounts. Accounts are audited by private external independent auditors appointed by the Board (Section 26(1)-(2) ISA). The SEC's current independent external auditor is one of the big four firms.

The SEC, not later than three months after the end of each year, submits to the minister of finance and the National Assembly, a report on its activities and administration during the immediately preceding year and, including in such reports, its audited accounts and the report of the auditor on the accounts. The assessors were provided with the SEC's 2011 audited accounts.

Apart from the above mentioned provisions, as far as the assessors were able to find out or were informed, there are no specific provisions in the ISA and in the SEC Rules and Regulations requiring the SEC to be transparent in its way of operation and use of resources or to make public its actions that affect users of the market, excluding confidential or commercially sensitive information.

#### *Code of Ethics*

The SEC Board members are required to subscribe to a Code of Ethics approved by the minister of finance (Section 12 ISA). It indicates the securities transactions that a member can engage in, restrictions in the purchase of securities, minimum holding period, notification of securities transactions, restrictions on beneficial interest, disclosure of interest in a particular company, report on investment holdings, and sanctions for violation of the Code of Ethics. A copy was provided to the assessors. It is not clear to the SEC staff who monitors compliance with it.

As explained in Principle 5, there is a Code of Conduct for Post-SEC Employment and a Code of Ethics for employees of the SEC. The Code of Conduct applies to all SEC employees, former employees, contract staff, IT staff and contractors engaged by the SEC. It contains sanctions. The Human Resources Department seems to be in charge of monitoring compliance with it. The Code of Ethics applies to all employees and contains disclosure requirements and trading prohibitions. The Commissioner of Finance and Administration receives the information and the Board of the SEC handles the sanctions for violation of the Code of Ethics.

The SEC has a whistle blowing policy. According to its Human Resources Policies and Procedures Manual the SEC is committed to delivering high quality services to its customers and it expects high standards from its employees. The whistle blowing policy is designed to encourage employees and contractors to raise concerns about malpractice within the SEC without fear of reprisal and to provide information about how to raise it.

|            |   |
|------------|---|
|            | <p><b>Review of the SEC's material actions</b></p> <p>There are various provisions in the ISA and the SEC Rules and Regulations that address procedural fairness, including in the Rules of Procedure of the APC. The requirement to provide reasons for the SEC's decisions is addressed through individual provisions in the ISA (see e.g., Sections 48(2)(c) and 122(12)(b)).</p> <p>Material actions of the SEC in applying its rules are subject to review by the IST (Section 289 ISA). The IST is a body of ten persons appointed by the minister of finance for a term of five years for the chairman and four years for the other nine members. They can be removed only for due cause (Part XVI ISA). It is the exclusive court of law in Nigeria to exercise jurisdiction to hear and determine any question of law or dispute involving, among others, a decision or determination of the SEC in the operation and application of the ISA and, in particular, relating to any dispute, among others, between an issuer, a Capital Market Operator, an investor or an SRO and the SEC.</p> <p>The IST is active and operational.</p> <p>It is mandatory to include in the arbitration clause (if any) in any underwriting agreement that any party aggrieved by the decision of the SEC may refer the matter to the IST (Rule 256). Parties affected by the SEC's decisions have remedies indicated in the ISA.</p> <p>Affected persons are permitted to make representations before a decision is taken by the SEC. The SEC provides the regulated entities with an opportunity to be heard. It has what is called an all parties meeting where the person allegedly not in compliance with the ISA is allowed to be heard.</p> <p>The accountability of the SEC is through the requirement to submit a report on its activities and administration during the immediately preceding year to the minister of finance and the National Assembly (including in such reports its audited accounts and the auditor's report on the accounts). The information provided is not of a confidential nature nor is it commercially sensitive information. Appeals on the IST's decisions can be made to the Court of Appeal and the Supreme Court. There is no issue of confidentiality with respect to information provided in a judicial process. The SEC's financial statements are audited by private sector auditors bound by professional secrecy. The SEC's Annual Reports are due to be available on its website; however the relevant section of the website was not accessible during the assessment mission due to maintenance. The Code of Ethics and the Code of Conduct were not available on the SEC's website during the mission. After the mission, a short extract of the SEC staff manual, which makes reference to the Code of Ethics, has been published.</p> |
| Assessment | Partly Implemented  |
| Comments   | <p>The SEC is not fully independent of government. The minister of finance may issue directives to the SEC with which the SEC must comply. The minister of finance is empowered to authorize persons to be exempted from provisions of the ISA. The treatment of the SEC is different for example from the National Pension Commission. The Pension Reform Act, 2004 does not contain provisions similar to the ones in the ISA with respect to the regulator's independence.</p> <p>In addition to the potential use of the legal powers provided to the minister of finance, any politically motivated involvement of the Senate in the operations of the SEC could also undermine its independence.</p> <p>The SEC has been without a Board since June 16, 2012. The terms of the members ended simultaneously without a prior preparation for the nomination of the Board as contemplated in the ISA. The new members of the Board must be confirmed by the Senate. The Senate is currently in recess. The SEC Board is necessary, among other things, to approve rules and regulations and to apply sanctions.</p> <p>If the SEC is required to repatriate ₦15 billion from its accumulated fund to the CRF account it will be left with ₦8 billion in reserves. If it continues to have budget deficits and will not in the future have enough funds in its accumulated fund to cover its deficits, the situation could raise concerns about its capacity to operate adequately due to resource constraints.</p> <p>The SEC does not have an ethics officer. Its provisions regarding ethics lack proper monitoring</p>   |

|                     |   |
|---------------------|---|
|                     | and enforcement. Transparency could be improved further by more formal publication of actions.  |
| <b>Principle 3.</b> | The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.  |
| Description         | <p><b>Sufficiency of SEC's powers and authorities</b></p> <p>The powers and authorities of the SEC are sufficient to meet its responsibilities, taking into account the nature of Nigeria's securities market and a full assessment of the IOSCO Principles.</p> <p><b>Funding</b></p> <p>The SEC's revenue in 2011 was ₦6,895,403,000 obtained mainly from market transaction charges and money market investment and bond interest income. The SEC expends most of its revenues in staff salaries and administrative expenses. It has the power to affect the operational allocation of its resources. As noted above in Principle 2, in 2011 the SEC had a deficit with respect to its funding. It had to use its accumulated fund.</p> <p><b>Level of resources and difficulty of attracting and retaining experienced and skilled staff.</b></p> <p>According to the SEC's 2011 annual report, its workforce at the end of the year was composed of 630 members of staff spread across four directorates and seven zonal offices.</p> <p>The percentage of staff in each Directorate of the four member Executive Management Committee is as follows:</p> <ul style="list-style-type: none"> <li>• The Director-General has 12 percent of the staff;</li> <li>• Executive Commissioner in charge of Operations has 29 percent of the staff;</li> <li>• Executive Commissioner in charge of Finance &amp; Administration has 25 percent of the staff; and</li> <li>• Executive Commissioner in charge of Legal &amp; Enforcement has 14 percent of the staff.</li> </ul> <p>The core disciplines of the staff are: economists (56), accountants (52), lawyers (67), computer scientists (15), mathematicians and statisticians (6) and others (402). 30 percent of the staff is involved with core disciplines while the other 70 percent is involved in other disciplines. According to the SEC staff, this represents a change from previous periods when 20 percent of the staff was involved in core disciplines and 80 percent in other disciplines.</p> <p>407 members of staff are regulars in a senior position. 16 members of staff are under contract in a senior position. 145 members of staff are regulars in a junior position. 20 members of staff are under contract in a junior position.</p> <p>The age distribution of the SEC staff shows that more than 50 percent of the staff is between the ages of 35 and 44 years. Less than 10 percent of the staff is between the ages of 25 and 29 years old.</p> <p>The remuneration (including allowances) and the terms and conditions of service of the Secretary and other staff of the SEC are determined by the Board of the SEC. The SEC is not under obligation to ask for approval of its staff remuneration from any other agency. Every staff member of the SEC is entitled to pension and other retirement benefits (Sections 16 and 18 of the ISA). The staff turnover is low and, according to the person responsible for human resources, the current turnover does not constitute a problem to the SEC.</p> <p>In discussions with market participants, it was indicated that the self-funded status that the SEC enjoys has not transformed into it using its resources to draw the best talent from the securities market.</p> <p><b>Adequacy of ongoing training</b></p> <p>According to the SEC annual report 2011, it expended around 10 percent of its 2011 revenues in</p> |

|                              | <p>training. Its staff has received different types of training in several areas. The list of courses provided showed ongoing training and the curricula were very broad and varied. The SEC has a training philosophy stated in its Human Resources Policies and Procedures Manual. There is a training plan and courses have included risk management and IFRS. However, some SEC staff members indicated that in some instances approval for technical training had been denied for budgetary reasons.</p> <table border="1"> <thead> <tr> <th>Types of Structured Training</th> <th>2012 Expenditure (₦ as at June 30, 2012)</th> <th>2011 Expenditure (₦)</th> </tr> </thead> <tbody> <tr> <td>In-House Training</td> <td>37,965,000.00</td> <td>15,000,000.00</td> </tr> <tr> <td>Local Training</td> <td>171,113,305.00</td> <td>142,620,400.00</td> </tr> <tr> <td>Foreign Training</td> <td>367,232,590.00</td> <td>516,436,000.00</td> </tr> <tr> <td><b>Total</b></td> <td><b>576,310,895.00</b></td> <td><b>674,056,400.00</b></td> </tr> </tbody> </table> <p>Source: SEC Annual Report (for 2011) and SEC staff (for 2012)</p> <p><b>Policies and governance practices</b></p> <p>The SEC has produced, and they are available to the public on its website, different forms and templates so anyone can use them to request services at the SEC. However, when asked about the procedures of the SEC to perform its core functions and exercise its powers, several of the persons interviewed made reference to practices without reference to specific written policies or procedures. A lack of written policies and procedures and reliance on manual, paper-based processes leads to inefficiencies in the SEC's processes and makes them prone to errors and potential misconduct. The SEC has ongoing projects aimed at improving its IT infrastructure, but the projects have been subject to serious delays.</p> <p><b>Investor education</b></p> <p>The SEC is involved in investor education and the training of all categories of intermediaries in the securities industry (Section 13(s) ISA). The SEC has a section on its website dedicated to investor education.</p> | Types of Structured Training | 2012 Expenditure (₦ as at June 30, 2012) | 2011 Expenditure (₦) | In-House Training | 37,965,000.00 | 15,000,000.00 | Local Training | 171,113,305.00 | 142,620,400.00 | Foreign Training | 367,232,590.00 | 516,436,000.00 | <b>Total</b> | <b>576,310,895.00</b> | <b>674,056,400.00</b> |
|------------------------------|---|------------------------------|--|----------------------|-------------------|---------------|---------------|----------------|----------------|----------------|------------------|----------------|----------------|--------------|-----------------------|-----------------------|
| Types of Structured Training | 2012 Expenditure (₦ as at June 30, 2012)  | 2011 Expenditure (₦)         |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| In-House Training            | 37,965,000.00   | 15,000,000.00                |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| Local Training               | 171,113,305.00  | 142,620,400.00               |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| Foreign Training             | 367,232,590.00  | 516,436,000.00               |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| <b>Total</b>                 | <b>576,310,895.00</b>   | <b>674,056,400.00</b>        |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| Assessment                   | Broadly Implemented   |                              |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| Comments                     | <p>Certain core regulatory competencies (e.g., on-site supervision of registered entities) do not appear to be well represented among the current SEC staff, even though the SEC's manpower is large vis-à-vis the current size and level of development of the Nigerian securities market. Even though increased over the past few years, the proportion of staff engaged in the core regulatory and supervisory functions is still only 30 percent. Several market participants informed the assessors that they consider important that the SEC concentrates on technical training for its personnel. It was mentioned that in practice private sector employees are generally not interested in working at the SEC. It is also rare for the SEC employees to move to the private sector. Market participants highlighted that there were what was called pockets of respect and expertise at the SEC, but in general terms the SEC needs to improve the technical capacity of its personnel.</p> <p>The SEC also needs to accelerate its plans to develop the technology infrastructure indispensable to adequately supervise the securities market. The same applies to increasing the use of IT in its internal processes. The SEC needs to have in place written procedures to conduct its operations</p>  |                              |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| <b>Principle 4.</b>          | The regulator should adopt clear and consistent regulatory processes.   |                              |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |
| Description                  | <p><b>Clear and equitable procedures</b></p> <p>The SEC is subject to the ISA which contains reasonable procedural rules and to the SEC Rules and Regulations which contain more detailed procedures. However the SEC does not appear to have any internal written policies and procedures on how it conducts its functions other than the Human Resource Policies and Procedures Manual.</p> <p><b>Process for consultation</b></p> <p>The SEC in the exercise of its powers to make rules must consult with stakeholders. The need to</p>   |                              |  |                      |                   |               |               |                |                |                |                  |                |                |              |                       |                       |

consult is established by law (Section 313(2)(2) ISA). The consultation process itself is not well established. It was described orally by several persons interviewed during the mission; however no written procedure appears to exist.

The process of consultation according to the ISA should be with stakeholders, but in practice it is carried out mostly with the Capital Market Operators. The SEC has a Rules Committee which handles the process of establishing new rules and regulations. New proposals for rules are discussed with the relevant Capital Market Operators. They are published for public comment (exposed). The SEC also uses advisory committees and informal contacts to support its rule making. The objective of the consultation process as applied by the SEC has been to provide participants in the capital market with notice of what is expected from them, what conduct will be sanctioned and to promote fairness and equality of treatment.

The SEC has prescribed rules and regulations. They are made of twelve parts and nine schedules, 312 rules as amended up to 2008 and 25 rules and amendments from 2008 until April 2012. They contain both rules of general and specific application governing securities exchanges; Capital Market Operators; securities offered for sale or subscription; mergers, acquisitions and combinations; collective investment schemes; investors protection fund; borrowing by States, local government and other government agencies amongst other things.

The SEC has improved the content of its website making it more investor friendly. Important information, such as the ISA and the SEC Rules and Regulations, is available to the public; however exposed rules are not permanently available for review and comment on the SEC's website. Currently the content of the final consolidated rules and regulations has not been updated with those that have been amended since 2008. This creates confusion to the public and the legal risk of not knowing which the rules and regulations currently in force are and what the responsibilities of the SEC are (see Principle 1). The rules and regulations are in the process of being consolidated.

The assessors were not able to obtain any documents regarding the explanation of the SEC's policies in important operational areas, such as setting of standards, or issuance of opinions stating the reasons for regulatory actions other than selected press releases provided by the SEC staff interviewed. The reasons for changes in rules are included as information provided in the introduction to the new rules and regulations.

The SEC has the authority to prepare guidelines and organize training programs and disseminate information necessary for the establishment of securities exchanges and capital trade points (Section 13(f) ISA). The concept of a guideline is not defined in the ISA. The only guideline currently available at the SEC's website deals with the Code of Conduct for Capital Market Operators and their Employees which is however also included in the Schedule of the SEC Rules and Regulations.

#### **Cost of compliance with regulation**

There are no specific evaluations done by the SEC about the cost to market participants of compliance with a rule or regulation before it is proposed by the SEC, however the persons interviewed at the SEC believe that the process of consultation with the market participants provides the SEC the feedback to determine the issue of cost of compliance with the proposed rule or regulation.

The rules and regulations are available to the public as indicated before, with the caveat of having a mix of current regulations with regulations that have been amended, which could create confusion to the reader. The rule-making procedure is not readily available to the public.

#### **Procedural fairness**

There are various provisions in the ISA and the SEC Rules and Regulations that address procedural fairness, including in the Rules of Procedure of the APC. The requirement to provide reasons for the SEC's decisions is addressed through individual provisions in the ISA (see e.g., Sections 48(2)(c) and 122(12)(b)).

Material actions of the SEC in applying its rules are subject to review by the IST (Section 289 ISA). The IST is working properly and has reviewed numerous SEC actions.

The IST is a body of 10 persons appointed by the minister of finance. The chairman is appointed for a term of five years. For the other nine members the term is four years. They can be removed only for due cause (Part XVI of the ISA).

It is the exclusive court of law in Nigeria to exercise jurisdiction to hear and determine any question of law or dispute involving, among others, a decision or determination of the SEC in the operation and application of the ISA, and in particular, relating to any dispute, among others, between an issuer, a Capital Market Operator, an investor or an SRO and the SEC. The IST is active and operational.

It is mandatory to include in the arbitration clause (if any) in any underwriting agreement that any party aggrieved by the decision of the SEC may refer the matter to the IST (Rule 256).

#### **Judicial review of the SEC's decisions**

Any person dissatisfied with a decision of the IST may appeal to the Court of Appeal. An appeal to the decision of the Court of Appeal must go to the Supreme Court.

#### **Criteria for granting, denying or revoking a registration**

There are established criteria to grant, deny or revoke a registration.

In cases where the SEC has assumed control of a Capital Market Operator whose paid-up capital is lost or unrepresented by available assets, it has the authority to make an order revoking the Capital Market Operator's registration (Section 51(a) ISA).

The SEC may suspend or cancel the registration granted to a Capital Market Operator or any registered function where the Capital Market Operator contravenes any of the provisions of the ISA, the SEC Rules and Regulations, or the Code of Conduct for Capital Market Operators and their Employees; fails to furnish any information relating to its activities as required by the SEC or furnishes information which is false and misleading in any material particular; fails to submit periodic returns or reports as required by the SEC, to co-operate in any enquiry or inspection conducted by the SEC, to update its systems and procedures as recommended by the SEC to resolve the complaints of clients; to give a satisfactory reply to the SEC in this regard; or to meet the renewal requirements for registration.

The SEC may cancel the registration granted to a Capital Market Operator where it is found guilty of fraud or repeated defaults or has been convicted of an offence involving moral turpitude (Rule 20B). Currently, due to the lack of a Board, the SEC's authority to revoke registrations, as well as any other sanction imposed by the APC needs to be approved by the minister of finance (Rule 17 of the Rules on APC Procedures as amended in March 2010).

The general criteria for granting, denying, or revoking a registration are published in the ISA and the SEC Rules and Regulations. The parties affected by the process are entitled to a hearing with respect to the SEC's decision.

#### **Procedures for making investigation reports public and rights of individuals, including confidentiality**

There is no specific provision in the ISA or the SEC Rules and Regulations regarding making reports on investigations public. The SEC's personnel are bound by an oath of secrecy. Investigations are not made public; however the SEC publishes on its website a list of companies facing enforcement action. The list includes the name of the company, the nature of the enforcement action and the reason why the action was taken.

|                     |  |
|---------------------|--|
|                     | <p><b>SEC's exercise of its powers and discharge of its functions</b></p> <p>From the information obtained by the assessors during interviews with the SEC's personnel and selected market participants, the SEC has not exercised its powers and discharged its functions consistently in the past. The different SEC departments do not appear to communicate adequately.</p>  |
| Assessment          | Partly Implemented   |
| Comments            | <p>There is no written procedure for the SEC's consultation process. The SEC's main concern in the consultation process is market participants and not necessarily the general public. The use of the website in the consultation process is limited.</p> <p>The establishment of the Investments and Securities Tribunal constitutes a positive corrective action.</p> <p>In the current situation in the absence of the Board for more than three months the final decision on the imposition of any sanctions to Capital Market Operators would need to be taken by the minister of finance. At the time of the assessment mission, no such decisions had been made by the minister.</p> <p>The assessors were informed of an instance where the SEC Rules and Regulations that were still in the process of consultation (exposed) had been used as if they were the rules in force (see Principle 24).</p>  |
| <b>Principle 5.</b> | The staff of the regulator should observe the highest professional standards, including appropriate standards of confidentiality.  |
| Description         | <p><b>Code of Conduct and Code of Ethics</b></p> <p>A Code of Conduct for the SEC employment exists. It is somewhat misleadingly called Code of Conduct for Post-SEC Employment. However it applies to all SEC employees, former employees, contract staff, NYSC, IT staff and contractors engaged by the SEC. There is also a Code of Ethics for the Board of the SEC and a Code of Ethics for the Staff of the SEC.</p> <p>The Code of Conduct for Post-SEC Employment contains a duty of confidentiality, certain conflicts of interest provisions, permanent restriction on representation on particular matters, two year restriction concerning particular matters under official responsibility and sanctions for non-compliance which include disciplinary action including dismissal and total withholding of benefits (financial or otherwise) that an employee would ordinarily have been entitled to. The SEC could bring action in court against former employees and may seek an order restraining the person from engaging in the conduct prohibited under the Code of Conduct.</p> <p>In addition to the Code of Conduct, Rule 4 of the SEC Rules and Regulations imposes an obligation of non-disclosure of information obtained in performing official duties. Every officer or employee of the SEC must adhere to a Code of Secrecy in respect of any paper, document or information which he/she may possess or have knowledge of, whether in the course of any examination or investigation conducted pursuant to any provision of the ISA or the SEC Rules and Regulations or in the course of official duty.</p> <p>SEC employees are subject to what is called an oath of secrecy that must be renewed every year.</p> <p><b>Appropriate use of information obtained in the course of the exercise of powers and discharge of duties</b></p> <p>Section 112(1)-(2) of the ISA contains certain prohibitions for a public officer to deal with certain securities. A public officer means any person working in the public service of the Federation or of a State as defined in the Constitution of Nigeria. The prohibitions of Section 112(2) are subject to certain appropriate exceptions set out in Section 113 of the ISA.</p> |

**Disclosure of financial affairs or interests and restriction on the holding or trading in securities**

Under the Code of Ethics, employees are prohibited from transacting in securities and investments which are subject to a registration statement filed under the provisions of the ISA before the effective date of registration and before opening of the offer for sale/subscription to the general public and in securities and investments of companies that are subject of investigation by the SEC or that are involved in any proceeding before the SEC.

According to the Code of Ethics, employees are prohibited from maintaining accounts with the securities firms. Securities purchased by an employee must be held for a minimum of six months before any sale. This restriction does not apply to units of CIS, unit trusts or any other security which has a maturity at the time of issuance of less than one year.

Any securities transaction by an employee must be reported to the Commissioner in charge of Finance and Administration. Employees of the SEC are not allowed to have a beneficial interest in any company registered with the SEC, except where such companies are publicly quoted. An employee must disclose his or her interest in any company in which he or she is a shareholder, if assigned to handle the registration application or anything affecting the company.

Employees must report every purchase or sale of any secondary market security within five working days of consummation of the transaction. Employees must also report receipt of notice of any change in holding resulting from inheritance, gifts, bonus issue and allotments of shares in the case of primary market issue. Employees having no interest in securities are required to so state.

Every employee must furnish the Commissioner of Finance and Administration on a form provided by the SEC information relating to securities owned by the employee or held for his or her benefit, by any trust or estate of which he or she is a trustee and by immediate family members who are partners or officers of securities firms, investment advisers, broker dealers and other Capital Market Operators registered by the SEC.

**Investigation and resolution of alleged violations of the SEC Code of Ethics**

The procedure for the implementation of the Code of Ethics is not clearly defined and it was not possible to verify how the Code is implemented.

In the case of the Code of Ethics for the SEC Board members there are requirements for disclosure of interests in a particular company, restriction on purchase of securities, a minimum holding period, requirements for notification of securities transactions, and restriction on beneficial interest. Members of the SEC Board are prohibited from maintaining accounts with securities firms.

**Sanctions for non-compliance**

Breaches of the Code of Conduct are subject to disciplinary action, including dismissal and total withholding of whatever benefits the employee would ordinarily have been entitled to. In case the breach of the Code of Conduct occurs after the cessation of employment, the SEC is entitled to bring action in court against any such person and to seek an order restraining the person from engaging in the conduct prohibited by the Code of Conduct. Sanctions for breaches of the Code of Ethics are not clearly indicated in the Code of Ethics.

The assessors were informed that monitoring compliance with the Code of Conduct is handled by the Human Resources Department; however the procedure is not clearly stated in a written document. The Code of Ethics for employees gives a role to the Commissioner of Finance and Administration as well as to the Board of the SEC. The SEC staff indicated that the Code of Conduct would have been applied in the past, but no specific examples were presented. The staff was not clearly aware of the Code of Ethics, the obligation to disclose information to the SEC and

|                     |  |
|---------------------|--|
|                     | <p>the trading restrictions applicable to staff.</p> <p>A proposal for a Code of Conduct for financial regulators has been discussed at the FSRCC. It includes disclosure requirements. The proposal has not yet been approved.</p>  |
| Assessment          | Partly Implemented   |
| Comments            | <p>Requirements for the disclosure of financial interests and restrictions on holding or trading in securities by the SEC staff are defined in the Code of Ethics for Staff of the SEC. The financial information of the SEC staff must be provided to the Commissioner (Finance and Operations); however in the discussions conducted with the heads of department it was indicated that they were not aware of this obligation. There is no clear procedure to monitor compliance with the Code of Conduct and the Code of Ethics. This implies that the Code of Ethics is in practice not implemented and enforced.</p> <p>The proposal for a Code of Conduct for financial regulators presented to the FSRCC covers the main aspects of a more robust ethics program.</p>  |
| <b>Principle 6.</b> | The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.  |
| Description         | <p><b>The SEC is not a systemic risk regulator</b></p> <p>The SEC does not conduct any analysis on systemic risks possibly arising from securities markets. There is no top down analysis of the macroeconomic (national or international) environment and its impact on the Nigerian securities markets. The supervisory information available to the SEC for example on solvency and liquidity of Capital Market Operators is so limited that it is not used to assess their possible impact on financial stability. Such an analysis could be used by senior management to determine whether there are important risks that need to be monitored.</p> <p><b>Contribution to the overall assessment of financial stability</b></p> <p>The SEC is a member of the FSRCC, which is an inter-agency body set up to deal with matters of common interest and concern to the various regulatory and supervisory authorities of the financial services industry. The FSRCC was accorded legal status by the 1998 amendment to Section 38 of the CBN Act 1991 and it was formally inaugurated in May 1999.</p> <p>The FSRCC was initially not a particularly active inter-agency body. It has become more active in the last three years.</p> <p>The objectives of the FSRCC do not specifically refer to systemic risk and financial stability. They are to:</p> <ol style="list-style-type: none"> <li>Coordinate the supervision of financial institutions, especially conglomerates;</li> <li>Cause the reduction of arbitrage opportunities usually created by differing regulatory and supervisory standards among supervisory authorities in the financial services industry;</li> <li>Deliberate on problems experienced by any member in its relationship with any financial institution;</li> <li>Eliminate any information gap encountered by any regulatory agency in its relationship with any group of financial institutions;</li> <li>Articulate the strategies for the promotion of safe, sound and efficient practices by financial intermediaries; and</li> <li>Deliberate on such other issues as may be specified from time to time.</li> </ol> <p>The FSRCC has resumed its meetings during the past three years. There is an MoU signed among its members. Discussions seem to be helping the members of the FSRCC to have a more comprehensive view of the problems, issues and risks across the different sectors of the financial</p> |

|                     |   |
|---------------------|---|
|                     | <p>sector. Exchange of information on the entities under the supervision of the various FSRCC members is addressed in the FSRCC MoU and facilitated through a section of the FSRCC website available only to the members of the FSRCC.</p> <p><b>Expertise</b></p> <p>The SEC is currently starting to develop expertise regarding risk measurements and analysis relevant to systemic risk. In addition it has been able to take into consideration risk measurements and analysis developed by other regulators. It is neither clear nor evident how these considerations have been applied in practice. There is on-going capacity building on risk-based supervision, where the potential systemic impact of a Capital Market Operator is planned to be taken into account in the decision on appropriate supervisory measures.</p>   |
| Assessment          | Partly Implemented  |
| Comments            | The level of expertise available at the SEC to conduct analysis on systemic risks possibly arising from securities markets or the implications that the macro-economic environment has on the securities market is currently limited. The FSRCC does not yet appear to be very focused on analyzing the potential sources of systemic risks, but has rather concentrated on coordinating micro-prudential initiatives (e.g., on consolidated supervision)   |
| <b>Principle 7.</b> | The Regulator should have or contribute to a process to review the perimeter of regulation regularly.   |
| Description         | <p><b>Internal assessment of perimeter of regulation</b></p> <p>The SEC does not have a specific process explicitly with the objective of assessing whether the securities regulatory framework adequately identifies and manages the risks posed by markets, participants and products to the ISA objectives, which are the protection of investor, fair, efficient and transparent markets and the reduction of systemic risk.</p> <p>The SEC has the power to conduct research into all or any aspect of the securities industry and advise the minister of finance on all matters relating to the securities industry (Sections 13(z)(aa) and (cc) of the ISA).</p> <p>There are supervisory programs in place for the capital markets operators with off-site and on-site inspections. The Monitoring &amp; Investigations Department reports that no on-site inspection took place in 2011. The off-site information is not well suited to help to identify potential areas of risk and contribute to determining if additional measures are needed.</p> <p>The identification of potential regulatory gaps is done on an ad hoc basis. Inputs can come from the market participants with topics of concern, from the Directors of departments, when they identify issues and bring them to the attention of the Executive Management Committee for further escalation to the Director-General and the Board.</p> <p>The SEC has a Rules Committee to review, where it is presented with information on changing circumstances, its past regulatory policy decisions on products, markets, entities, market participants or activities, especially decisions to exempt, and take measures as appropriate. The Rules Committee is composed of 15 members including staff members of the SEC as well as market participants. It is chaired by the office of the SEC Secretary. The Director of the Legal Department is involved.</p> <p>The proposed rules are evaluated by the different departments at the SEC. They are sent to the SEC management for approval and exposure. Extracts of the proposed rules are published in two national papers and the full proposals are posted on the SEC web page.</p> |

|   |   |
|---|---|
|   | <p>Actions could involve imposing additional requirements on Capital Market Operators or issuers, providing guidance or making proposals for change in the law.</p> <p>Examples of the identification of risks which ended in the establishment of rules and regulations are: Rules on Market Makers (April 2012); Rules on Securities Lending and Borrowing; Rules on Exchange-Traded Funds; Rules on Custodial Services for Registered Collective Investment Schemes (January 2011); and SEC CBN Rules on Margin Lending (October 2010).</p> <p>The SEC participates in a process (with other financial system supervisors and regulators if appropriate), which reviews unregulated products, markets, market participants and activities, including the potential for regulatory arbitrage, in order to promote investor protection and fair, efficient and transparent markets and to reduce systemic risks. This is done through collaboration with the FSRCC and other agencies. The SEC has also contributed to the detection of ponzi schemes, wonder banks and similar illegal activities by referring cases it has detected to the criminal authorities.</p> <p>The SEC seeks legislative or other changes when it identifies a regulatory weakness or risk to investor protection, market fairness, efficiency and transparency that requires legislative or other changes (Section 313(1) of the ISA). There have been no recent changes in the ISA which was enacted in 2007.</p>   |
| Assessment  | Broadly Implemented   |
| Comments  | The rule making process could be streamlined at the initial stage by establishing specific deadlines to produce the proposals that are required to ensure that any gaps in the regulatory framework are promptly addressed.   |
| <p><b>Principle 8.</b> The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.</p> |   |
| Description   | <p><b>Overview on the treatment of conflicts of interest and misalignment of incentives</b></p> <p>The SEC does not have a specific process in place designed to identify and evaluate potential and actual conflicts of interest and misalignment of incentives. The Nigerian regulatory framework includes some requirements for the identification, monitoring and mitigation of conflicts of interest, but there is some variation in the content of the requirements depending on the type of regulated entity. In some cases the requirements do not apply to the entity itself, but rather to its employees.</p> <p>The Nigerian securities regulatory framework also uses trading prohibitions in some cases to address conflicts of interest. In other cases, as for example with issuers, the disclosure to the public is used as a tool to address the conflict of interest.</p> <p><b>Capital Market Operators</b></p> <p>Fund managers are subject to the requirement to avoid conflicts of interest (Section 157(1)(a)). There is no requirement to disclose conflicts of interest. Rule 247 of the SEC Rules and Regulations addresses certain conflicts of interest through trading prohibitions applicable to the management company, trustee and their affiliates (see Principle 24).</p> <p>A management company, trustee and their affiliates are subject to a prohibition from dealing as principals in the sale of underlying assets to the trust scheme; prohibition of deals in, or retention of any underlying securities of any company, if those individual officers of the management company or any of their affiliates own each beneficiary more than 0.5 percent of the securities of such company and together more than 5 percent of the securities of that particular company; and a provision prohibiting the fund manager from investing in its in-house, trustee's or their associates' instruments (Rule 247).</p> <p>The Code of Conduct for Capital Market Operators and their Employees (Schedule IX SEC Rules</p> |

|   |   |
|---|---|
|   | <p>and Regulations) that in Nigeria applies also to credit rating agencies and sell-side analysts establishes the need for avoidance of conflicts of interest by employees who must ensure that their personal interest does not at any time conflict with their duty to their employer's clients. There is a requirement to disclose all the personal interests beneficial or not of the employee. The information must be disclosed to the employer. However the Code of Conduct does not apply to the Capital Market Operator itself, but only to its employees.</p> <p><b>Auditors</b></p> <p>The SEC Code of Corporate Governance states that, in addition to its statutory functions, the audit committee has the following responsibilities regarding auditors' independence:</p> <ul style="list-style-type: none"> <li>• Assist in the oversight of the integrity of the company's financial statements, compliance with the legal and other regulatory requirements, assessment of qualifications and independence of external auditor.</li> <li>• Review the independence of the external auditors and ensure that where non-audit services are provided by the external auditors there is no conflict of interest.</li> <li>• Preserve auditor independence, by setting clear hiring policies for employees or former employees of independent auditors.</li> </ul> <p>In order to safeguard the integrity of the external audit process and guarantee the independence of the external auditors companies should rotate both the audit firms and audit partners.</p> <p><b>Issuers</b></p> <p>The issuer must disclose in the prospectus any existing and potential related party transactions and conflicts of interest in relation to the company and its related parties, together with steps taken to resolve such conflicts of interest; the nature and extent of the related party transactions and conflict of interest situations; declaration of an expert on any existing and potential interests/conflicts of interest in any capacity vis-à-vis the company/group.</p> <p><b>Disclosure of director's interest in stock broking/dealing companies</b></p> <p>A director of a public company must disclose to the SEC any interest he/she has in stock broking/dealing companies engaged by the company to which he is a director (Rule 112).</p> <p><b>Disclosure of interest of stock broking/dealing companies in quoted companies</b></p> <p>Stock broking/dealing companies must disclose their interest in publicly quoted companies in offer documents as well as in their Annual Report and accounts (Rule 113).</p> <p>For an issuer in a take-over bid, disclosure of potential conflicts of interest needs to be provided. For example the director's circular issued by the director of the offeree company must include particulars of any payment made to an officer or former officer of an offeree company by the way of compensation for loss of his/her office or as consideration for or in connection with his/her retirement from any office (Section 140 of the ISA).</p> |
| Assessment  | Broadly Implemented   |
| Comments  | The SEC does not have an overarching requirement for the avoidance, management and disclosure of conflicts of interest applicable to regulated entities.  |
| <b>Principles for Self-Regulation</b>   |   |
| <p><b>Principle 9.</b> Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.</p> |   |

|             |  |
|-------------|--|
| Description | <p><b>SROs in Nigeria</b></p> <p>The SEC is required to promote and register SROs, including securities exchanges, capital trade points and capital market trade associations to which it may delegate its powers (Section 13(o) ISA). According to Article 315 of the ISA, a self-regulatory organization means any registered securities exchange, capital trade point, and association of securities dealers, clearing house, capital market trade association or any other self regulatory body approved as such by the SEC. The self-regulatory role of securities exchanges and capital trade points derives also directly from Section 29 of the ISA, that sets certain self-regulatory responsibilities as a precondition for the registration of a securities exchange or capital trade point (see Principle 33). These responsibilities include the requirement to establish and enforce binding rules of trading and business conduct as well as establish disciplinary rules and conduct disciplinary proceedings.</p> <p>The interpretation of Section 315 would appear to be that in addition to securities exchanges and capital trade points, all associations of securities dealers, clearing houses and capital market trade associations would be self-regulatory bodies. However, none of these bodies are defined in the ISA, and the SEC Rules and Regulations refer to National Association of Securities Dealers (not to associations of securities dealers in general) and securities clearing and settlement companies (not to clearing houses). Further, the SEC has not yet officially delegated its powers to any capital market trade association as referred to in Section 13(o) or approved any other self-regulatory body so that it would have become an SRO.</p> <p>Rule 23 of the SEC Rules and Regulations includes registration requirements for a national association of securities dealers. The requirements imply that such a body would be created for the purpose of operating a trading platform. The NASD Ltd owned by the members of the Nigerian Association of Securities Dealers was granted an Approval-in-Principle in September 2012 for registration of an OTC market under Section 29 of the ISA (see Principle 33 on the definition of a securities exchange that also covers an OTC market).</p> <p><b>Authorization of SROs</b></p> <p>The requirements for the authorization of a securities exchange or capital trade point are described under Principle 33. These requirements include some of the elements of Key Question 2(a), but some gaps remain. There are no specific requirements for the regulator to assess the capacity of the SRO to carry out the purposes of the governing laws, regulations and SRO rules, and to enforce compliance with them. There is no requirement for the SROs to promote investor protection, and the rules of the SROs are not required to be consistent with the public policy objectives established by the regulator. There are no requirements for the SROs to cooperate with the SEC to investigate and enforce applicable laws, regulations and rules.</p> <p>In addition to the above, the regulatory framework does not include any requirements for fair treatment of members and applicants for membership. In practice, there are currently no rules on admission of new members and admission criteria in the NSE. According to the information provided on the website of the NSE, membership is granted to broker-dealers to enable them to use the services of the NSE and broker-dealers must meet specific requirements set by the NSE to receive a dealing member license. These requirements are said to be detailed in the Application Requirements for Dealing Membership License document available from the NSE's Legal Department, which was not available for review during the mission. In practice the NSE has not admitted new members for several years.</p> <p>There is no requirement for the SROs to have MoUs or other formal arrangements in place to secure cooperation between them and the SEC. There is no MoU between the SEC and the NSE, nor have they otherwise formally agreed on any particular arrangements for their cooperation. In practice the cooperation of the SEC and NSE in e.g., dealing member supervision is limited, and is largely based on the quarterly reports that the NSE sends to the SEC. The Monitoring &amp; Investigations Department of the SEC that is responsible for the supervision of broker-dealers does not have any contacts with the NSE, but the communication is organized through and the reports received by the Registration and Recognized Investment Exchanges Department.</p> <p>The SROs are not under a regulatory obligation to avoid rules that may create anti-competitive</p> |
|-------------|--|

|            |  |
|------------|--|
|            | <p>situations. The NSE does not appear to have such rules, and its policy of not admitting new members has effectively created an anticompetitive situation. Finally, there are no requirements on the SROs to avoid using their oversight role to allow any market participant to gain advantage in the market in an unfair manner.</p> <p>The NSE's self-regulatory functions are described in Principles 33-34.</p> <p>The requirements in Rule 23 of the SEC Rules and Regulations relating to an application for registration of a national association of securities dealers are very similar to those applicable to a securities exchange, with the exception of the fact that an association is not required to provide listing requirements (because it cannot operate a listing market). The ISA does not include any requirements on the self-regulatory tasks of an association registered as an SRO since Section 29 applies only to securities exchanges and capital trade points. Rule 23 refers to a code of conduct, code of dealing, instruction and inspection manual of members' activities and a requirement to enforce compliance by the SRO's members with the provisions of the ISA and SEC Rules and Regulations.</p> <p><b>Oversight by the SEC</b><br/>The oversight program of the SEC in the NSE is covered in Principle 34.</p> <p>Section 32(3) of the ISA specifically provides that nothing precludes the SEC from carrying out inspections, or conducting enquiries or audits of any member of a securities exchange, capital trade point or other self-regulatory organization, i.e., the SEC retains full authority to inquire into matters affecting the investors or the market.</p> <p>According to Section 33 of the ISA, where a self-regulatory organization reprimands, fines, suspends, expels or otherwise takes disciplinary action against its member, it must within seven days notify the SEC in writing of the name and other particulars of the member and the nature of and reason for the action taken. On the basis of Section 34 of the ISA, the SEC may review any disciplinary action and may affirm or set aside such decision after giving the member and self-regulatory organization an opportunity of being heard. Nothing precludes the SEC from suspending, expelling or otherwise imposing or causing disciplinary action to be taken against a member where the self-regulatory organization fails to act, provided that, before exercising this power, the SEC gives the affected member and the self-regulatory organization an opportunity of being heard.</p> <p><b>Professional standards</b></p> <p>The ISA, the SEC Rules and Regulations, or the SEC itself do not require the NSE or other self-regulatory organizations to follow any particular standards of behavior beyond those required from all registered entities. Therefore confidentiality and procedural fairness are not addressed, nor are there specific requirements for the appropriate use of information obtained in the course of the SRO's exercise of its powers and discharge of its responsibilities.</p> <p><b>Conflicts of interest</b></p> <p>Beyond the conflict of interest requirements included in Schedule IX.2 of the SEC Rules and Regulations applicable to employees of Capital Market Operators, there are no conflict of interest rules for SROs.</p> |
| Assessment | Partly Implemented   |
| Comments   | <p>Even though the Nigerian regulatory system makes use of self-regulatory organizations, the process for assigning a body as an SRO and the regulatory requirements on other types of SROs than securities exchanges and capital trade points are unclear. There are requirements on the SROs to inform the SEC of the disciplinary measures they have taken, and the SEC is not precluded from carrying out inspections of dealing members.</p> <p>Instead of assessing applications for registrations as a SRO on a case-by-case basis, the SEC should make a strategic decision on the role of various types of SROs in the regulation and supervision of Nigerian securities markets, and based on that, clearly define the responsibilities of various types of SROs in the regulatory framework.</p>  |

|  |  |
|--|--|
|  | In practice the SEC and NSE appear to coordinate and cooperate in their regulatory/self-regulatory activities only to a limited extent. It is recommended that the SEC and NSE increase the level of coordination of their activities, in particular to ensure that the large dealing member community is subject to robust supervision.   |
| <b>Principles for the Enforcement of Securities Regulation</b> |  |
| <b>Principle 10.</b>   | The regulator should have comprehensive inspection, investigation and surveillance powers.   |
| Description  | <p><b>SEC's inspection, investigation and surveillance powers</b></p> <p>The SEC has the power to call for information from and inspect as well as conduct inquiries and audits of securities exchanges, Capital Market Operators, collective investment schemes and all other regulated entities (Section 13(r) ISA). The SEC is not required by the ISA to give prior notice and the inspections can be done on-site. The SEC does not delegate this power to the NSE; instead, the NSE has its independent on-site inspection program (see Principle 34).</p> <p>The SEC is under the obligation to conduct routine and special inspections and investigations of any Capital Market Operator that is involved in the administration, management or custody of funds for or on behalf of clients including the management and operation of a collective investment scheme or the soliciting of investment in a collective investment scheme (Section 45(1) ISA). The Monitoring &amp; Investigations Department (M&amp;I) is in charge of monitoring, inspecting and investigating specific Capital Market Operators. It also investigates and resolves disputes among market stakeholders.</p> <p>The SEC must examine periodically the books and affairs of each Capital Market Operator, for which it has a right of access at all times to the books, accounts and vouchers of Capital Market Operators, and it is empowered to require from directors, managers and officers of Capital Market Operators such information and explanations as it may deem necessary to the performance of its duties.</p> <p>Every Capital Market Operator must produce to the SEC's examiners all books, accounts, documents and information which they may require. The SEC has the above mentioned power to obtain books and records and request information from Capital Market Operators without judicial actions even in the absence of suspected conduct and as indicated on a routine basis.</p> <p>The SEC has the power to conduct surveillance of trading activity at the NSE (see Principle 34).</p> <p>In the case of routine examinations the SEC forwards a copy of the report arising from the examination, together with the SEC's recommendations, to the Capital Market Operator with instruction that it be placed before the meeting of the board of directors of the Capital Market Operator specially convened for the purpose of considering the report and its recommendations (Section 46 ISA).</p> <p><b>Special examinations</b></p> <p>The SEC has the power to order a special examination or investigation of the books and affairs of a Capital Market Operator for any of the following reasons:</p> <ul style="list-style-type: none"> <li>• it is in the public interest to do so;</li> <li>• the Capital Market Operator has been carrying on its business in a manner detrimental to the interest of its clients, beneficiaries and creditors;</li> <li>• the Capital Market Operator has insufficient assets to cover its liabilities to the clients, beneficiaries and creditors;</li> <li>• the Capital Market Operator has been contravening the provisions of this Act; or</li> <li>• an application is made therefore by a director, shareholder, client, beneficiary or creditor of the Capital Market Operator.</li> </ul> <p>In the case of special examinations and investigations which are conducted for the reasons indicated above, the SEC must appoint one or more qualified persons other than SEC's officers to conduct the examination or investigation, under conditions of confidentiality, of the books and affairs of the Capital Market Operator (Section 47(1)-(2) ISA).</p> |

|  |   |
|--|---|
|  | <p>The SEC may conduct an investigation into the business of a person whether registered or authorized or not, who is involved in the administration of a CIS or the soliciting of investment in a CIS (Rule 172(1)).</p> <p><b>Obligation to maintain records</b></p> <p>A Capital Market Operator must keep or cause to be kept accounting and other records (Section 39(1) ISA). Capital Market Operators are required to maintain records concerning client identity and records that permit tracing funds and securities in and out of brokerage and bank accounts related to securities transactions. The SEC has the authority to have access to the identity of all clients of Capital Market Operators.</p>  |
| Assessment   | Fully Implemented   |
| Comments   | The regulatory framework grants the SEC the powers to conduct inspections and investigations. On the basis of the information gathered during the assessment, these powers have not been used in the past for several reasons including capacity issues. Currently the powers are being used more; however there is a lack of coordination among the SEC's departments which results in the SEC not acting timely or efficiently (see Principle 12).  |
| <b>Principle 11.</b> The regulator should have comprehensive enforcement powers. |   |
| Description  | <p><b>SEC's investigative and enforcement powers</b></p> <p>The functions and powers of the SEC related to investigation and enforcement (Section 13 ISA) are to:</p> <ul style="list-style-type: none"> <li>• protect the integrity of the securities market against all forms of abuses including insider dealing;</li> <li>• intervene in the management and control of a Capital Market Operator which it considers has failed, is failing or is in crisis including entering into the premises and doing whatsoever the SEC deems necessary for the protection of investors;</li> <li>• enter and seal up the premises of persons illegally carrying on capital market operations;</li> <li>• seek judicial order to freeze the assets (including bank accounts) of any person whose assets were derived from the violation of the ISA, or any securities law or regulation in Nigeria or other jurisdictions;</li> <li>• prevent fraudulent and unfair trade practices relating to the securities industry; and</li> <li>• disqualify persons considered unfit from being employed in any arm of the securities industry.</li> </ul> <p>In the case of a failing Capital Market Operator the SEC is authorized to (Section 48 ISA):</p> <ul style="list-style-type: none"> <li>• prohibit the Capital Market Operator from receiving funds or other assets from the public;</li> <li>• require the Capital Market Operator to take any steps or any action or to do or not to do any act or thing whatsoever, in relation to the Capital Market Operator or its business or its directors or officers which the SEC may consider necessary;</li> <li>• remove any manager or officer of the Capital Market Operator;</li> <li>• in respect of a Capital Market Operator remove from office any director, or appoint any person or persons to manage the affairs of the Capital Market Operator in the interim; and</li> <li>• appoint any person to advise the Capital Market Operator in relation to the proper conduct of its business.</li> </ul> <p>The SEC Board has the power to assume control of the whole property and affairs of a Capital Market Operator and to carry on the whole of its business and affairs (Section 49 of the ISA). The SEC has the power to revoke a registration or apply to Court to revoke a registration.</p> <p><b>Sanctions</b></p> <p>The SEC has the power to levy penalties on any person in relation to investments and securities business in Nigeria in accordance with the provisions of the ISA (Section 13(u) ISA).</p> <p>The ISA stipulates specific penalties for certain violations of the ISA. For example, a public company not having a system of internal control over its financial reporting, having an auditor that is not registered with the SEC and not disclosing within 20 days prior to the beginning of a quarter</p> |

to the NSE its quarterly earnings forecast is liable to a penalty of not less than ₦1,000,000 and a further penalty of ₦25,000 per day for the period the violation continues.

The general penalty applicable when there is no specific penalty consists of a fine of not less than ₦100,000 and a further sum of ₦5,000 per day for every day that the violation continues.

The SEC may in addition to any penalty prescribed under the ISA, direct any person who has contravened any of the provisions of the ISA or a related rule or regulation, to compensate any person who may have suffered any direct loss as a result of the contravention.

The SEC may also direct the forfeiture to the victim of any direct benefit or advantage received or receivable by the person in contravention.

In the exercise of its powers to impose a penalty, the SEC must accord the person in violation a fair hearing (Section 303(1) ISA).

#### **Administrative Proceedings Committee**

An Administrative Proceedings Committee (APC) exists for the purpose of hearing Capital Market Operators and institutions in the market that have allegedly violated any of the provisions of the ISA and the SEC Rules and Regulations and persons against whom complaints/allegations have been made to the SEC (Rule 312, Schedule VII SEC Rules and Regulations, Rule 3: Reference of matters to the Committee, Rules on APC procedures March 2010).

Complaints are forwarded to the SEC by the complainant. The complaint is investigated by the appropriate department which means the department for the time being responsible for investigation and enforcement in the SEC.

Where the appropriate department is of the opinion that any provision of the ISA, the SEC Rules and Regulations or the Code of Conduct for Capital Market Operators and their Employees has been violated, it prepares a report of the matter and formulates appropriate claim and details of the alleged violations and forwards them to the Secretary of the APC with all documents considered by the department.

The APC has jurisdiction, among others, in respect of the following:

- disputes between investors and Capital Market Operators;
- disputes between Capital Market Operators;
- disputes between securities exchanges, capital trade points and other SROs;
- disputes arising from public offers by companies;
- disputes between investors and issuers of securities;
- disputes between investors;
- disputes between SROs;
- violations or probable or threatened violation of the provisions of the ISA, the SEC Rules and Regulations and the Code of Conduct for Capital Market Operators and their Employees;
- violation of the Code of Corporate Governance for public companies;
- activities and dealings of public companies and their employees;
- issues relating to the registration of Capital Market Operators and SROs;
- public sale or trading in unregistered securities;
- dealing in securities or sale of securities to the public;
- unethical and unprofessional practice, manipulation and use of deceptive devices or contrivances in securities transactions;
- denial of registration;
- non-compliance with orders, guidelines and directives of the SEC; and
- any other matter which the SEC may direct it to hear.

It is possible for the parties to arrive at an inter-party settlement. Settlements must be acceptable to the APC. However settlements do not apply to matters initiated by the SEC or matters involving manipulation, insider dealing and any other serious violation to be determined by the SEC from time to time (Rule 10: Inter-Party Settlement as amended March 2010).

*APC's administrative sanctions*

The APC has the power to impose any of the following sanctions:

- suspension or cancellation of registration of a capital market operator;
- revocation of the certificate of a securities exchange or capital trade point;
- suspension or expulsion or other decisions/actions against members of securities exchanges, capital trade points and other SROs in respect of their members;
- suspension or expulsion or other decisions/actions against members/officials of securities exchanges, capital trade points and other SROs where they fail to act against their members/officials;
- removal of executive officers of a Capital Market Operator, securities exchange, capital trade point or other SROs;
- suspension of registration of securities;
- fines for late registration and non-compliance with the ISA, the SEC Rules and Regulations and the Code of Conduct for Capital Market Operators and their Employees;
- restitution and compensation orders;
- determination of compensation for insider dealing cases;
- disqualification of professionals or sponsored individuals from operating in the capital market;
- imposing conditions for registrations;
- imposing the rate of interest payable to subscribers by issuing houses for late return of monies;
- payment of administrative charges; and
- any other sanctions which the SEC may prescribe from time to time (Rule 16 Sanctions, Rules on APC Procedures as amended March 2010).

Every decision of the APC must be confirmed by the SEC Board before it becomes effective. However when there is no Board the decision must be confirmed by the minister of finance.

Any party who is not satisfied with the decision of the APC as confirmed by the SEC may appeal to the IST (Rule 13). The IST was put into operation in 2002. The IST provides a process for the resolution of securities markets related cases that do not have to be resolved in the regular court system. It has handled more than 400 cases, the breakdown of which into various types of cases was not available at the time of the assessment mission. The IST deals with the resolution of disputes in the securities market and the enforcement cases delivered by the SEC. It can provide to the SEC at its request remedies such as freezing assets, closing down firms involved in fraud, and appointing receivers.

#### **Suspension of trading**

The SEC may issue directives to a securities exchange, capital trade point or any other SRO. The SEC may suspend or prohibit further trading in securities (Sections 35(1) and 36(1) of the ISA). See Principle 36 on further details on the SEC's power to suspend trading.

#### **Information sharing with criminal prosecuting authorities**

Where in the course of its investigation, the SEC discovers evidence of possible criminality, the SEC passes such information to the appropriate criminal prosecuting authorities, such as the office of the Attorney-General of the Federation (AFG), the Attorney-General of a State or the Economic and Financial Crimes Commission (EFCC).

According to information provided by the SEC, the SEC has a list of 42 open cases referred to the Nigeria Police Force for criminal investigation. The nature of the offences includes fraudulent conduct, misappropriation of client's funds, and illegally operating in the market. The oldest case is from November 2002. In most of the 42 cases the SEC is awaiting for an update on the status of the case.

The SEC has referred cases relating to 21 Capital Market Operators to the EFCC. In the most serious case, there were 171 investors who had complained of unauthorized sales and non-purchase of clients' shares. The managing director of that particular Capital Market Operator was detained by the EFCC. No further report has been available to the SEC. In another case, there were 45 cases of capital market malpractices relating to the same Capital Market Operator. In another case dealing with unauthorized sale and non-purchase of securities paid for by various

clients' worth of ₦136 million, the managing director was tried, convicted and jailed for five years. For the other 19 Capital Market Operators, the cases involve offences such as illegally operating as a Capital Market Operator. The SEC is awaiting an update on the current status of the cases from the EFCC. One of the cases regarding illegally operating as a Capital Market Operator is before the High Court in Lagos. The oldest case referred to the EFCC is from September 2004. The most recent case referred is from August 2011.

The SEC had appealed to both the Nigeria Police Force and the office of the AGF to post some of their personnel to work with the SEC in the SEC's premises. As a result, the Nigeria Police Force has currently a unit with 19 police officers at the SEC headquarters in Abuja, collaborating with the SEC to investigate criminal infractions. The SEC believes that this will help to enhance the investigative and prosecutorial capabilities of the two agencies on fraudulent/criminal conduct in the Nigerian securities market. The SEC has also commenced local and foreign capital market related training of the police officers and the prosecutors from the office of the AGF.

The SEC has the power to investigate and to require and obtain information from any person, including third party entities and individuals (whether regulated or unregulated), that are either involved in relevant conduct or that may have information relevant to a regulatory or enforcement inquiry/investigation. It includes the power to obtain contemporaneous records sufficient to reconstruct all securities transactions, including records of all funds and assets transferred into and out of bank and brokerage accounts relating to those transactions.

The SEC has the power to call for, or furnish to any person, such information as may be considered necessary by it for the efficient discharge of its functions (Section 13(t) ISA).

#### **Records for securities and derivatives transactions**

A Capital Market Operator is under the obligation to keep its records in sufficient detail to show particulars of all monies received or paid by it, including monies paid to or disbursed from a trust account; all purchases and sales of securities made by the Capital Market Operator, the charges and credits arising from them, and the names of the buyers and sellers of each of those securities; all securities which are the property of the Capital Market Operator showing by whom the securities or the documents of title to the securities are held and, where they are held by some other person, whether or not they are held as securities against loans or advances; and all securities that are not the property of the Capital Market Operator and for which the dealer or any nominee controlled by the security dealer is accountable, showing by whom, and for whom, the securities or the documents of title to the securities are held and the extent to which they are either held for safe custody or deposited with a third party as securities for loans or advances made to the Capital Market Operator.

The records must be kept in sufficient detail to show particulars of every transaction by the capital market operator; specify the day on which or the period during which each transaction by the Capital Market Operator took place; and contain copies of acknowledgements of the receipt of securities or of documents of title to securities received by the Capital Market Operator from clients for sale or safe custody clearly showing the name or names in which the particular securities are registered. Derivative transactions are not common in Nigeria.

A securities exchange, capital trade point or any other self-regulatory organization must maintain proper books of account and records relating to its operations which must be made available for inspection by the SEC (Section 37 ISA).

A Capital Market Operator who contravenes or fails to comply with any of these provisions commits an offence and is liable on conviction to a fine of not less than ₦500,000 or to a term of imprisonment of not less than one year or to both such fine and imprisonment (Section 39(4) ISA).

The SEC can enter into a cooperative agreement with other regulators for the discharge of its functions (Section 13 ISA). The SEC can share information with other regulators obtained from its regulatory activities.

In practice with respect to obtaining banking information the SEC communicates with the CBN to obtain the information. The SEC has signed a MoU as member of the FSRCC. The SEC chairs the Information Sharing Committee of the FSRCC.

| Assessment  | Fully Implemented   |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
|---|---|---|--|--|-------------|-------------------------|---|------|----|------------|------|----|------------|------|---|------------|---------------------------------|--|--|-------------|---------------|----------------|------|---|---|------|---|---|------|---|--|
| Comments  | <p>The SEC has in the ISA sufficient legal tools to address the main violations in the Nigerian securities markets. The SEC's powers include the imposition of monetary sanctions. There is no maximum limit on the amount of sanction that the SEC can impose. Usually most jurisdictions establish by law, or by regulation, the maximum amount in case of monetary sanctions that a regulator can impose.</p> <p>According to some market participants the SEC has not used its enforcement tools adequately in the past. Allegations of instances of insider trading and market manipulation with no action taken by the SEC were mentioned by several of the market participants interviewed. Since 2010 there are indications that there is a change, however more concrete, effective and timely actions need to be taken. The SEC efforts to increase cooperation with the criminal authorities, including by training their staff and by having their representatives located in the SEC's premises are important steps in the right direction.</p>  |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| <b>Principle 12.</b> The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program. |   |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| Description   | <p><b>System of inspections</b></p> <p>The SEC must conduct an inspection to a registered person for compliance with regulatory requirements within one month of registration (Rule 46(1)).</p> <p>As per Rules 46 and 123 the SEC is empowered to inspect registered persons to ensure compliance with regulatory requirements on a periodic basis. This mandate is carried out by the Monitoring &amp; Investigations Department (M&amp;I) through on-site and off-site inspections. According to the information provided by the SEC staff interviewed, the M&amp;I Department reviewed in 2011 a total of 2,072 quarterly returns submitted by broker/dealers. Following analysis of the 2,072 returns, 18 firms were found to have reported shareholders' funds below regulatory minimum, nine firms were with negative shareholders' funds, 10 firms were assessed to have high 30-90 percent of their total assets as margin loans to clients, 26 firms were assessed to have between 40 percent to 96 percent of their total assets in unquoted equities, while 36 firms still had outstanding debt exposure to banks constituting between 31 percent to 682 percent of their total assets. Some other violations were also detected which imposed a high risk to the market. As a result the department selected for inspection during the first and second quarters of 2012 certain companies which were considered to have violated the rules. The request for approval of the schedule for the inspections from the department to management was presented in June 2012. Those inspections were started after the assessment mission.</p> <table border="1"> <thead> <tr> <th colspan="3"><b>SEC's Routine On-Site Prudential Inspections</b></th> </tr> <tr> <th><b>Year</b></th> <th><b>Number inspected</b></th> <th><b>Sanctions by penalties imposed (₦)</b></th> </tr> </thead> <tbody> <tr> <td>2009</td> <td>23</td> <td>34,622,809</td> </tr> <tr> <td>2010</td> <td>13</td> <td>52,027,432</td> </tr> <tr> <td>2011</td> <td>0</td> <td>95,582,263</td> </tr> </tbody> </table> <p>The sanctions imposed in 2011 came from off-site inspections, since no on-site inspections were conducted in 2011.</p> <table border="1"> <thead> <tr> <th colspan="3"><b>SEC's Target Inspections</b></th> </tr> <tr> <th><b>Year</b></th> <th><b>Number</b></th> <th><b>Remarks</b></th> </tr> </thead> <tbody> <tr> <td>2009</td> <td>6</td> <td>1 company was suspended for market manipulation</td> </tr> <tr> <td>2010</td> <td>1</td> <td>1 company was referred to EFCC for further criminal investigation</td> </tr> <tr> <td>2011</td> <td>1</td> <td></td> </tr> </tbody> </table> <p>The inspection and enforcement activities of the NSE are covered in Principle 34.</p> | <b>SEC's Routine On-Site Prudential Inspections</b>               |  |  | <b>Year</b> | <b>Number inspected</b> | <b>Sanctions by penalties imposed (₦)</b> | 2009 | 23 | 34,622,809 | 2010 | 13 | 52,027,432 | 2011 | 0 | 95,582,263 | <b>SEC's Target Inspections</b> |  |  | <b>Year</b> | <b>Number</b> | <b>Remarks</b> | 2009 | 6 | 1 company was suspended for market manipulation | 2010 | 1 | 1 company was referred to EFCC for further criminal investigation | 2011 | 1 |  |
| <b>SEC's Routine On-Site Prudential Inspections</b>   |   |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| <b>Year</b>   | <b>Number inspected</b>   | <b>Sanctions by penalties imposed (₦)</b>                         |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2009  | 23  | 34,622,809  |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2010  | 13  | 52,027,432  |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2011  | 0   | 95,582,263  |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| <b>SEC's Target Inspections</b>   |   |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| <b>Year</b>   | <b>Number</b>   | <b>Remarks</b>  |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2009  | 6   | 1 company was suspended for market manipulation                   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2010  | 1   | 1 company was referred to EFCC for further criminal investigation |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |
| 2011  | 1   |   |  |  |             |                         |   |      |    |            |      |    |            |      |   |            |                                 |  |  |             |               |                |      |   |   |      |   |   |      |   |  |

**Risk-based inspections**

The SEC is planning to move to a risk-based approach to supervision (see Principle 31).

**Complaints handling**

Currently the investors have a variety of authorities to which to bring a complaint including the SEC, NSE, IST, and EFCC. There is no clear guidance on how various categories of customer complaints and disputes will be handled. This results in a less than efficient process. The SEC's website has a section to be used by the public to send complaints. It is not clear if the SEC is informed of all the complaints received by other authorities.

In addition to the number of complaints brought forward from the previous year, the following table includes information on the complaints received and resolved by the SEC each year, those transferred internally to enforcement as well as the cases outstanding at the end of each year.

**Three-year Statistics of Complaints Management**

| <b>Details</b>   | <b>2009</b> | <b>2010</b> | <b>2011</b> |
|--|-------------|-------------|-------------|
| Complaints brought forward against stockbrokers, registrars and other Capital Market Operators | 999         | 926         | 664         |
| New complaints   | 695         | 1,223       | 729         |
| Resolved complaints  | 666         | 1,169       | 709         |
| Transfer to Enforcement & Compliance Department  | 102         | 316         | 156         |
| Outstanding complaints   | 926         | 664         | 528         |

The types of complaints lodged against broker-dealers include:

- unauthorized/fraudulent sale of shares;
- non-remittance of share sale proceeds;
- refusal/illegal transfer of shares;
- falsification of clients' accounts;
- non-purchase of shares/undue delay in purchase of shares; and
- non-verification of share certificates.

Complaints on non-remittance of share sale proceeds rose to their highest in 2010 largely due to the problem of margin facilities most brokers had with the banks and their clients. The trend changed in 2011 with the intervention of the SEC, the NSE and the Asset Management Corporation of Nigeria (AMCON).

The types of complaints lodged against registrars include:

- non-receipt of dividends;
- non-verification of share certificates;
- non-issuance of share certificates; and
- wrong crediting of accrued bonus shares.

As a result of the cases transferred to the Enforcement and Compliance Department, the following total amount of monetary sanctions were given. A total of 26 cases arising from complaints were referred to criminal action by the SEC.

**Enforcement and Compliance Department – Monetary Sanctions**

| <b>Type of case/market abuse</b>  | <b>2010 in ₦</b> | <b>2011 in ₦</b> | <b>2012 in ₦</b> |
|-----------------------------------|------------------|------------------|------------------|
| Insider information               | 0                | 0                | 0                |
| Market manipulation               | 0                | 0                | 0                |
| Other market abuse related topics | 33,217,000       | 33,094,500       | 21,123,143,84    |

| <b>Enforcement and Compliance Department – Referral to criminal action</b> |                  |                  |                  |
|--|------------------|------------------|------------------|
| <b>Type of case/market abuse</b>   | <b>2010 in ₹</b> | <b>2011 in ₹</b> | <b>2012 in ₹</b> |
| Insider information  | 0                | 0                | 0                |
| Market manipulation  | 0                | 0                | 0                |
| Other market abuses  | 11               | 9                | 5                |
| Other breach of SEC rules and regulations                                  | 1                | 0                | 0                |

As demonstrated by the above statistics, the SEC receives numerous complaints from investors. As a result its inspection and enforcement programs are expended on managing innumerable disputes between customers and brokers dealing basically with contractual disputes and unauthorized transactions. The process is time consuming and involves using too many resources.

**Market surveillance**

The SEC has no automated system to identify unusual transaction on the NSE. It maintains permanently two members of its staff on the premises of the NSE.

**Market and/or price manipulation and insider trading**

Manipulative and deceptive devices and contrivances are prohibited. A person involved in securities trading must not employ any device, scheme or artifice to defraud or capable of defrauding any person or institution; make, utter or present any untrue statement of a material fact; omit to disclose a material fact necessary in order not to render any statement misleading in the light of the circumstances under which the statement was made; engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person in connection with the purchase or sale of or dealing in any security; or deal in the securities of a company of which he is an insider.

Dealing by an insider applies to dealings at a recognized securities exchange and also to off-market dealings in securities, and occurs where a person or group of persons who is in possession of some confidential and price sensitive information not generally available to the public, utilizes such information to buy or sell securities for his/its own account and benefit or makes such information available to a third party (either knowingly or unknowingly) who uses it for his benefit. (Rule 110).

Rules and regulation regarding misrepresentation of material information or other fraudulent or manipulative practices relating to securities are in place. Rules and regulations against insider trading exist (Section 111–114 ISA and Rules 110–111 of SEC Rules and Regulation).

A person who is an insider of a company must not buy or sell, or otherwise deal in the securities of the company which are offered to the public for sale or subscription if he/she has information which he/she knows is unpublished price sensitive information in relation to those securities.

There is a definition of “insider” in Rule 110 of the SEC Rules and Regulations. It includes an individual who is connected with the company during the preceding six months in one of the following capacities: a director of the company or a related company; an officer of the company or a related company; an employee of the company or related company; a person in a position involving a professional or business relationship to the company; a shareholder who owns 5 percent or more of any class of securities; any person who can be deemed to be an agent of any of the above listed persons; and a person who by virtue of having been connected with the company has obtained unpublished price sensitive information in relation to the securities of the company.

The SEC has issued a Code of Conduct for Capital Market Operators and their Employees to address failure of compliance with the conduct of business requirements. It contains sanctions.

**Requirements for firms’ compliance systems**

The SEC requires regulated entities to have in place supervisory and compliance procedures reasonably designed to prevent securities law violations. A compliance officer must be appointed

by every capital market operator. The compliance officer must be registered by the Capital Market Operator with the SEC as a sponsored individual. The compliance officer must immediately and independently report to the SEC any non-compliance observed by him/her (Section 61 and 63 ISA, Rule 168(b) on appointment of compliance officer). Personnel from the Monitoring & Investigations Department were not aware of any report to the SEC by a compliance officer since 2006 (see Principle 31).

It is not clear how the SEC actually monitors how compliance procedures are executed and communicated to employees of Capital Market Operators.

The SEC does not take measures against or discipline or sanction Capital Market Operators for failure to reasonably supervise subordinate personnel whose activities violate the securities laws.

The SEC requires market surveillance mechanisms that permit an audit of the execution and trading of all transactions made on the NSE.

### **Effectiveness**

The SEC is building its enforcement program in order to enforce securities laws.

Investigations are conducted by the Monitoring & Investigations Department. After an investigation is finished, the case is transferred to the Enforcement and Compliance Department that conducts a review of the case in order to confirm the possible violations of the ISA or the SEC Rules and Regulations. The mentioned departments report to the Executive Commissioner Legal and Enforcement. From the Enforcement and Compliance Department the matter is then taken to the Executive Commissioners and the Director General for approval to take the case to the APC.

As indicated in Principle 1 the APC is a quasi-judicial body established by Section 310 of the ISA. It is formed by non-executive SEC Commissioners, directors of departments, representatives from the Ministry of Finance and the CBN. Trade associations in the capital market participate in the APC but they do not vote.

The APC convenes a hearing with the parties and witnesses. Evidence is taken and arguments are presented. The APC issues a recommended decision to the SEC Board. According to Section 310(3) of the ISA final decisions by the APC must be sent to the SEC Board for confirmation. The SEC Board makes a final decision based on the APC's decision. The SEC Board decision can be appealed to the IST.

On the basis of the information reviewed by the assessors and discussions with the SEC personnel, the SEC's enforcement system does not in practice appear to be effective for several reasons. Firstly, it was not possible to confirm whether there is a proper audit trail of all the cases that the various SEC departments have investigated and that have then possibly been passed on to the Enforcement & Compliance Department and from there possibly to the criminal process. The involved departments do not seem to communicate directly, but the communication takes place through the senior management. Secondly, onsite inspections are currently not done on a routine basis, and there have been severe delays in the decisions to take action in potential enforcement cases.

However, the SEC has worked to improve its enforcement capabilities. It has obtained assistance from a foreign regulator to build its enforcement capacity and has outsourced several enforcement actions. Specifically, as a result of the CBN intervention in several banks after the crisis of 2008 the SEC and the CBN worked together in a Joint Task Force (JTF) in 2010. The JTF included private law firms and an audit firm. It was set up to identify deviations from the ISA and relevant SEC Rules and Regulations. The JTF identified infractions such as false trading and market rigging, price fixing transactions, general fraud liability and insider trading. The SEC has filed five cases at the IST in respect of banks intervened by the CBN. The suits included the banks and their directors and subsidiaries. Four suits started in the middle of 2010 and one was filed in 2011. The alleged violations of several ISA provisions include insider trading and manipulative devices. The SEC seeks various remedies for the series of infringements complained of, including certain injunctive as well as declarative reliefs. To handle the cases the SEC hired external counsel. One of the cases was discontinued following the federal government directive that instructed the attorney-general to enter into plea bargains with the affected banks. The suit was dismissed in October

|   |                          |  |
|---|--------------------------|--|
| <p>2011. The other four cases are still pending at the IST.<br/>The following table describes the status of the SEC's enforcement action as at March 2011 as presented on the SEC website</p>   |                          |  |
| <b>Companies Facing Enforcement Action (as at March 2011)</b>   |                          |  |
| <b>Number of companies</b>  | <b>Type of sanctions</b> | <b>Reason</b>  |
| 39  | 34<br>Suspensions        | Yet to pay penalty for non-remittance of quarterly returns (28)<br>Unethical capital market conduct (6)  |
|   | 5 licenses<br>revoked    | Unauthorized sale of clients shares (3)<br>Failure to pay client return on investment and principal (1)<br>Breach of share purchase and resell agreement with client (1)   |
| <p>Out of the above 39 companies, six have since closed business. 33 cases are still pending. Oldest case still pending dates back to 2009.</p> <p>The only other statistics that consolidated the enforcement actions taken by the SEC are presented below. They relate to the measures taken by the Collective Investment Schemes Department.</p> |                          |  |
| <b>Summary of Fund Managers Referred for Enforcement Action</b>   |                          |  |
| <b>Year</b>   | <b>Number</b>            | <b>Nature of Violation</b>   |
| 2010  | 4                        | <ul style="list-style-type: none"> <li>• Commingling of fund's assets; misappropriation/borrowing of fund's money; failure to keep proper records.</li> <li>• Mismanagement of the schemes.</li> <li>• Operation of unauthorized funds.</li> <li>• Issuance/dealing in additional unregistered units of the schemes</li> </ul> |
| 2011  | 1                        | Failure to provide requisite information on the assets of the fund and remit same to the trustee   |
| 2012  | 1                        | Mismanagement of the fund.   |
| <b>Sanctions for Late/Non-Submission of Statutory Returns with Respect to CIS</b>   |                          |  |
| <b>Year</b>   | <b>Number</b>            | <b>Amount of fine (₦)</b>  |
| 2010  | 17                       | 4,019,000  |
| 2011  | 5                        | 3,278,500  |
| 2012  | 2                        | 174,000  |
| Total   | 24                       | 7,471,500  |
| <b>Number of Sanctions and Nature of Violations/Misconduct with Respect to CIS</b>  |                          |  |
| <b>Year</b>   | <b>Number</b>            | <b>Nature of Violation</b>   |
| 2010  | 7                        | <ul style="list-style-type: none"> <li>• Late filing of accounts.</li> <li>• Late filing of monthly and quarterly returns.</li> </ul>  |
| 2011  | 9                        | Late filing of accounts  |
| 2012  | 15                       | <ul style="list-style-type: none"> <li>• Late filing of accounts.</li> <li>• Non submission of accounts</li> </ul>   |
| <p>The lack of aggregate information on the total amount and nature of enforcement measures taken by the SEC appears to reflect the lack of internal procedures and governance practices referred to under Principles 3 and 4.</p>  |                          |  |
| Assessment  | Partly Implemented       |  |

|  |  |
|--|--|
| Comments   | <p>On the basis of the several discussions conducted with the personnel in charge of enforcement as well as the review of the information provided, there appear to be significant challenges with the efficiency and efficacy of the SEC’s enforcement. This is affected by the division of the functions of investigations and enforcement among the different departments of the SEC and the lack of procedures to govern the processes and keep track of the progress of cases. The result is the absence of a satisfactory control over the cases. The SEC should improve the audit trail of cases transferred internally from one department to another and from the SEC to criminal authorities.</p> <p>The SEC’s resources are being use to tackle minor violations. They should be re-deployed to address more serious violations in the securities market.</p> <p>A potential conflict of interest is possible due to the composition of the APC. The mere presence of a member of a trade association in the APC meetings, although without voting right, could create potential conflicts of interest</p> <p>To address the current lack of effectiveness of its enforcement function, the SEC has outsourced the enforcement of a group of important cases handled by a Joint Task Force with the CBN to private law and audit firms. The cases are pending at the IST.</p>   |
| <b>Principles for Cooperation in Regulation</b>  |  |
| <b>Principle 13.</b> The regulator should have authority to share both public and non-public information with domestic and foreign counterparts. |  |
| Description  | <p><b>Domestic information sharing and co-operation</b></p> <p>Section 13(y) of the ISA allows the SEC to relate effectively with domestic regulators and supervisors of other financial institutions, including entering into co-operative agreements on matters of common interest. The SEC can share with domestic regulators and supervisors of other financial institutions any information that they need to perform their functions.</p> <p>Section 13(y) of the ISA does not limit the type of information that can be shared. It also does not require any external approval for the sharing of information.</p> <p><b>International information sharing and cooperation</b></p> <p>Section 13(y) of the ISA allows the SEC to relate effectively with foreign regulators and supervisors of other financial institutions including entering into co-operative agreements on matters of common interest. The SEC can share with foreign regulators and supervisors of other financial institutions any information that they need to perform their functions.</p> <p>There are no limitations to the type of information that the SEC can share, and the sharing of information does not require any external approval.</p> <p><b>Unsolicited information</b></p> <p>There is no explicit recognition in Section 13(y) of the ISA that the SEC may send information to foreign regulators and supervisors without the existence of a prior request. However the SEC has the power to call for, or furnish to any person, such information as may be considered necessary by it for the efficient discharge of its functions (Section 13(t) ISA).</p> <p><b>Requirement for breach of domestic laws</b></p> <p>The SEC can share information and cooperate with other foreign regulators and supervisors even in cases in which the investigated conduct does not constitute a breach of Nigerian law.</p> <p><b>Bank account information</b></p> <p>There is no explicit recognition in Section 13(y) of the ISA that allows the SEC to share information about the beneficial ownership of bank and brokerage accounts. Although there is no explicit recognition, Section 13(y) relating to the SEC’s power to enter into co-operative agreements on matters of common interest with foreign regulators is broad enough to allow the SEC to share</p> |

|  |  |
|--|--|
|  | <p>information about the beneficial ownership of banking and brokerage accounts.</p> <p>According to Section 13(x) of the ISA, the SEC may seek judicial order to freeze the assets (including bank accounts) of any person whose assets were derived from the violation of the ISA, or any securities law or regulation in Nigeria or other jurisdictions.</p> <p><b>Confidentiality</b></p> <p>There is no explicit requirement in Section 13(y) of the ISA that the confidential information gathered by the SEC that is shared with another competent authority has to be subject to appropriate rules of confidentiality. However, confidentiality is addressed both in the IOSCO MMoU and, on the basis of one bilateral MoU reviewed, in the bilateral information sharing arrangements.</p>  |
| Assessment   | Fully Implemented  |
| Comments   |  |
| <b>Principle 14.</b> Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts. |  |
| Description  | <p><b>Power to enter into information sharing agreements</b></p> <p>There is no explicit provision that authorizes the SEC to enter into information sharing agreements with domestic and foreign authorities, but according to the SEC such authority is implicit in the power to enter into co-operative agreements on matters of common interest with domestic and foreign regulators conferred by Section 13(y) of the ISA.</p> <p><b>Information sharing mechanisms</b></p> <p><i>Domestic authorities</i></p> <p>The SEC is a member of the Financial Services Regulation Coordinating Committee (FSRCC). The FSRCC is an inter-agency body set up to deal with matters of common interest and concern to the various regulatory and supervisory authorities in the financial services industry. The FSRCC was accorded legal status by the 1998 amendment to Section 38 of the CBN Act 1991 and it was formally inaugurated in May 1999.</p> <p>The FSRCC was not initially an active inter-agency body. It has become more active in the last three years, including through the preparation of several important proposals that however still have to be approved. For example, a proposal for a Code of Conduct for Financial Regulators first presented for discussion in 2009 has not yet been approved.</p> <p>The objectives of the FSRCC are to:</p> <ol style="list-style-type: none"> <li>Coordinate the supervision of financial institutions, especially conglomerates;</li> <li>Cause the reduction of arbitrage opportunities usually created by differing regulatory and supervisory standards among supervisory authorities in the financial services industry;</li> <li>Deliberate on problems experienced by any member in its relationship with any financial institution;</li> <li>Eliminate any information gap encountered by any regulatory agency in its relationship with any group of financial institutions;</li> <li>Articulate the strategies for the promotion of safe, sound and efficient practices by financial intermediaries; and</li> <li>Deliberate on such other issues as may be specified from time to time.</li> </ol> <p>The current members of the FSRCC as specified by Section 43(2) of the CBN Act 2007 are:</p> <ul style="list-style-type: none"> <li>The governor, CBN (chairman);</li> <li>The managing director, NDIC;</li> <li>The director-general, SEC;</li> <li>The commissioner for insurance, NAICOM;</li> </ul> |

- The registrar-general, Corporate Affairs Commission (CAC);
- A representative of the federal ministry of finance (FMF) not below the rank of a director (currently the director, Home Finance);
- The director-general, PENCOTM;
- The director-general, NSE (observer);
- The managing director of the Abuja Securities and Commodity Exchange (ASCE) (observer); and
- The executive chairman of the Federal Inland Revenue Service (observer).

The FSRCC has five standing Sub-Committees. One of the Sub-Committees is the Information Sharing Sub-Committee (ISSC). Its responsibilities include identifying the type of information and the mechanism and procedures for information sharing, resolving conflicts in information sharing, and recommending measures to guard against misuse of information. The ISSC is chaired by the SEC.

To give effect to the foregoing, all FSRCC members have signed a Memorandum of Understanding (MoU) on the type of information to be shared among members only. The MoU is being revised to include financial system stability indicators and statistics.

The information to be shared is cascaded into two levels. The first level of information is available to some designated management staff of member agencies while the Chief Executive Officers of member agencies have access to both the first and second levels of information.

The FSRCC also has ad-hoc committees. One of the ad-hoc committees is the Consolidated Supervision Committee. On March 19, 2009, the FSRCC set up an Inter-Agency Committee to prepare a framework and work out the modalities and timelines for implementing consolidated supervision of financial institutions in Nigeria. The Inter-Agency Committee prepared a draft Framework for Consolidated Supervision which was presented at the July 14, 2011 meeting of the FSRCC.

#### *Foreign counterparts*

The SEC has been a signatory to the IOSCO MMoU since 2006. It has also entered into nine bilateral MoUs with foreign regulators. The MoUs have been signed with South Africa, Ghana, Tanzania, China, Uganda, India, Malaysia, Kenya and Mauritius. After the end of the assessment mission, the SEC published on its website a list of the bilateral MoUs signed with foreign regulators. It is currently also negotiating MoUs with Oman and Zambia.

#### **Confidentiality**

As described under Principle 13, there is no explicit requirement in Section 13(y) of the ISA that the confidential information gathered by the SEC that is shared with another competent authority has to be subject to appropriate rules of confidentiality. However, confidentiality is addressed both in the IOSCO MMoU and, on the basis of one bilateral MoU reviewed, in the bilateral information sharing arrangements. More specifically, as signatory to the IOSCO MMoU, the SEC can maintain the confidentiality of the request for information received from a foreign regulator.

#### **Practice**

All members of the FSRCC have signed an MoU on the type of information to be shared among members only. In practice, the information sharing is implemented through a common database that includes information on registered entities, sanctions given and fitness and propriety assessments.

Consolidated information on the precise number of requests for assistance received by the SEC from foreign authorities was not available during the assessment mission, even though the staff mentioned instances where the SEC had received requests for assistance under the IOSCO MMoU. According to the information provided after the mission, the SEC has provided investigatory or enforcement assistance to two foreign regulators under the IOSCO MMoU.

|  |  |
|--|--|
| Assessment   | Broadly Implemented  |
| Comments   | The SEC needs to improve the coordination of the handling of the requests for assistance by foreign regulators made under the different MoUs. As one of the 86 signatories to the IOSCO MMoU and with nine bilateral MoUs signed, the SEC must be in a position to attend to all the requests received and keep track of the assistance provided. The need for better coordination in this area is closely linked to the SEC's need to improve the audit trail of enforcement cases that it deals with internally or passes on to the criminal authorities (see Principle 12).   |
| <b>Principle 15.</b> The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers. |  |
| Description  | <p><b>Records</b></p> <p>As noted in Principle 10, Section 13(r) of the ISA provides that the SEC has the power to call for information from, inspect, and conduct inquiries and audits of securities exchanges, Capital Market Operators, collective investment schemes and all other regulated entities. This broad power covers records and information about securities and derivatives transactions (the latter are rare in the market); bank and brokerage accounts; and details about clients of securities firms, including the identity of the ultimate account holders.</p> <p>Section 13(y) of the ISA allows the SEC to relate effectively with foreign regulators including entering into co-operative agreements on matters of common interest.</p> <p><b>Compliance with laws and regulations</b></p> <p>The SEC can seek information and documents relating to all matters within its jurisdiction. This includes market abuse, the issuance of securities, Capital Market Operators (market intermediaries) and markets, exchanges and clearing and settlement facilities.</p> <p><b>Independent interest</b></p> <p>There is no requirement for the SEC to have an independent interest in a matter in relation to which a foreign regulator seeks assistance.</p> <p><b>Information on regulatory processes</b></p> <p>The SEC can provide information about regulatory processes, including the authorization process, investigations in progress and sanctions imposed.</p> <p><b>Documents and statements</b></p> <p>The SEC can use its evidence gathering powers under the ISA to require information and documents requested by a foreign regulator. The SEC's powers under the ISA include the power to summon a person and take a statement from them. As an administrative body, the SEC does not have the power to request the taking of a person's statement under oath.</p> <p><b>Court orders</b></p> <p>The SEC can request the IST to issue court orders.</p> <p><b>Financial conglomerates</b></p> <p>The powers available to the SEC under the ISA mean it is able to seek documents and information about financial conglomerates on a foreign regulator's behalf.</p> <p><b>Information from other domestic authorities</b></p> <p>The SEC can seek information from other domestic authorities in response to a request from a foreign authority.</p> |

|  |   |
|--|---|
|  | <p><b>Use of information</b></p> <p>As signatory to the IOSCO MMoU, the SEC is subject to Art. 10(a) of the MMoU. On the basis of one bilateral MoU reviewed, the bilateral MoUs signed by the SEC require that the information to be shared is used for performing the tasks entrusted to competent authorities</p>  |
| Assessment   | Fully Implemented   |
| Comments   | <p>During the mission, the assessors experienced difficulties in obtaining exact information about how many requests had been received under the IOSCO MMoU and other MoUs signed by the SEC. The information is not appropriately managed and stored. Consideration should be given to designating experienced personnel with enforcement background or from the Enforcement and Compliance Department to handling the matters related to international enforcement cooperation.</p> <p>The SEC keeps the content of the MoUs it has signed confidential. International best practices suggest that other securities regulators show greater transparency than is currently the case with the SEC, since their MoUs are published on their websites. After the mission, the SEC published the list of the bilateral MoUs it has signed on its website. However, there could be even greater transparency and reporting of its cooperative endeavors, which should benefit the image of the country and its financial sector.</p>   |
| <b>Principles for Issuers</b>  |   |
| <b>Principle 16.</b> There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions. |   |
| Description  | <p><b>Market overview</b></p> <p>Public quoted companies, public unquoted companies, governments and government agencies and investment schemes need to register their securities and file reports with the SEC.</p> <p>Private companies looking to list their shares on the NSE must comply with the listing rules and requirements of the NSE. The NSE has two boards in the Equities Market: the Main Board and the Alternative Securities Market (ASeM) Board. Corporate debt products such as corporate bonds and preference shares are listed on one of the two boards in the Debt Market.</p> <p>Fund managers may also list their investment funds on the exchange. Investment funds are not actively traded on the NSE. They are listed on the List of Memorandum Quotations Market to provide the investing public access to their daily prices.</p> <p>The types of business entities that would be eligible to list their securities on the NSE are:</p> <ul style="list-style-type: none"> <li>• Large Nigerian companies: The Main Board comprises large companies with at least 300 shareholders, 20 percent of share capital on offer to the public, and the ability to raise an unlimited amount of capital.</li> <li>• Small-to-medium Nigerian enterprises (SMEs): The ASeM comprises SMEs with at least 51 shareholders, 15 percent of share capital on offer to the public, and the ability to raise an unlimited amount of capital.</li> <li>• Foreign companies (overseas issuers). There must also be a signed Memorandum of Understanding (MoU) between the NSE and the company's home country exchange to ensure all available means of natural process for investor protection.</li> <li>• Investment Trusts (Units): An investment trust is a separate legal person or company constituted under a trust deed that has a fund manager, trustee (ensures the fund manager keeps to the fund's investment objective and safeguards the trust assets), unit holders (have the rights to the trust assets), distributors (allow the unit holders to transact in the fund manager's unit trusts), and registrars (usually engaged by the fund manager and generally act as middlemen between the fund manager and various other stakeholders).</li> <li>• Investment Trusts (Real Estate): A Real Estate Investment Trust (REIT) is a tax designation for a corporate entity investing in real estate that is intended to reduce or eliminate corporate income taxes. REITs are typically required to distribute 90 percent of their income into the</li> </ul> |

hands of the investors. REITs can be publicly or privately held.

#### **Disclosure requirements for issuers**

The ISA and the SEC Rules and Regulations contain clear and comprehensive disclosure and reporting requirements for issuers whose securities are offered to the public.

#### *Prospectus for public equity and debt offers*

The Mandatory contents of the prospectus include (Section 73, Schedule 111 ISA):

- the company's proprietorship, management and capital requirement;
- property acquired or to be acquired by the company;
- contracts;
- auditors;
- interests of directors;
- accountants' report;
- five year historical financial information stating the accountant's report, accounting policies, balance sheets, profit and loss accounts, cash flow and notes to the accounts. If the company has existed for less than five years, audited historical financial information for the number of years in existence or an audited statement of affairs for a new company;
- caveat on risk factors;
- risk factors;
- definitions and corporate directory;
- description of group structure;
- expected timeframe for completion of project period;
- information about the company;
- information on shareholders/Directors/key management staff;
- related party transactions/conflicts of interest;
- director's interests;
- merger or take-overs;
- financial information - segmental reporting;
- accountant's report;
- property schedule;
- financial and non-financial disclosure requirements;
- directors' remuneration;
- confirmation of the "going concern status";
- corporate governance compliance;
- pledge of assets;
- capacity utilization;
- research and development; and
- disclosure of developments/events occurring after submission of prospectus but before opening the offer.

The prospectus and the annual report must state the level of compliance with the Code of Corporate Governance. According to this Code the question whether a company or entity is required to comply with or to observe the principles or provisions of the code of corporate governance must be, in the first instance, determined by the Board and shareholders and thereafter by the SEC.

Whenever the SEC determines that the Code of Corporate Governance is breached by a company or entity required to comply with or observe its principles or provisions, the SEC must notify the company or entity concerned specifying the areas of non-compliance or non-observance and the specific action or actions needed to remedy the non-compliance or non-observance. So far the SEC has not taken any such measures.

The regulatory framework requires financial information and other required disclosures in prospectuses, listing documents, and annual and other periodic reports to be of sufficient timeliness to be useful to investors.

#### *Annual reports*

Every public company whose securities are required to be registered must file with the SEC on a periodic or annual basis and on a specified format its audited financial statement and other returns as may be prescribed by the SEC from time to time.

Every public company must appoint a compliance officer who in conjunction with the Chief Financial Officer must ensure compliance with all regulatory requirements of the SEC.

The annual report to be filed with the SEC must in all material facts comply with the provisions of the IFRS issued by the FRC. The annual reports must be filed with the SEC not later than 90 days after the financial year end in line with the provisions of CAMA

The Chief Executive Officer and Chief Financial Officer or Officers or persons performing similar functions in a public company must, in filing the annual account, attach a duly signed certification letter certifying in each annual or periodic report filed, that:

- The public company has established a system of internal controls over its financial reporting and security of its assets and it must be the responsibility of the board of directors to ensure the integrity of the company's financial controls and reporting.
- The board of directors of a public company has reported on the effectiveness of the company's internal control system in its annual report.

The auditor of a public company must in his audit report to the company issue a statement as to the existence, adequacy and effectiveness or otherwise of the internal control system of the company.

Any company who fails to file its annual report with the SEC is liable to a fine of ₦1 million and the sum of ₦25,000 for every day the default continues.

Periodic information about financial position and results of operations are made publicly available to investors.

#### *Quarterly report*

Public quoted companies must not later than 30 days from the end of each quarter file with the SEC and simultaneously with the NSE and the investing public a quarterly report prepared in accordance with the IFRS. The quarterly report must contain the following by way of notes:

- a) Accounting policy changes;
- b) Seasonality or cyclical nature of operations;
- c) Unusual items;
- d) Changes in estimates;
- e) Issuance, repurchase, and repayment of debt and equity securities;
- f) Dividends;
- g) Items of segment information (for those entities required by SAS 24 and IAS 14 to report segment information annually);
- h) Significant events after the end of the interim period;
- i) Business combinations;
- j) Long term investments;
- k) Restructuring and reversals of restructuring provisions;
- l) Discontinuing operations;
- m) Correction of prior errors;

- n) Write-down of inventory to net realizable value;
- o) Impairment loss of property, plant, equipment, intangible or other assets, and reversal of such impairment loss;
- p) Litigation settlements;
- q) Any debt default or any breach of a debt covenant that has not been corrected subsequently;
- r) Related party transactions;
- s) Acquisitions and disposals of property, plant and equipment; and
- t) Commitments to purchase property, plant and equipment.

The Chief Executive Officer and Chief Financial Officer or Officers or persons performing similar functions in a public company must in filing the quarterly report attach a duly signed certification letter.

All public companies must publish their "signed" quarterly balance sheet, income statement and cash flow statements in at least one national daily newspaper. However, the accounting policies, notes and other relevant information must be posted on the company's website which address must be disclosed in the newspaper publication. The publication must be signed by the CEO and the CFO.

Any company which fails to file its quarterly report with the SEC must be liable to a fine of ₦1 million and the sum of ₦25,000 for every day the default continues.

#### **Half yearly returns**

Public companies must file with the SEC half yearly returns which must include:

- a) General information;
- b) Corporate governance issues;
- c) Financial reporting;
- d) Unclaimed dividends;
- e) Audit Committee;
- f) Undertaking by the company secretary, chief internal auditor, financial controller, managing director, Board chairman, and chairman of Audit Committee certifying the reliability of the information in the format provided.

The completed form must be returned to the SEC within 30 days from the end of the half year period, either in hard or electronic copy.

Any company which fails to file its half yearly returns with the SEC is be liable to a fine of ₦1 million and the sum of ₦25,000.00 for every day the default continues.

#### **Earnings forecast**

All public companies must release their earnings forecast to the NSE, the SEC and the investing public 20 days prior to the commencement of a quarter. The forecast must be certified by the chief executive officer and chief financial officer.

#### **Audit Committee**

Every public company must establish an Audit Committee with written terms of reference. The Committee must be independent in carrying out its terms of reference. The Audit Committee must maintain records of attendance and deliberations of its meetings and interactions.

The Audit Committee of every public company must review the company's financial statements prior to approval by the Board of the company and present the report at the Annual General Meeting.

**Risk management by public companies**

All public companies must include risk management as part of their accounting policies and, by way of notes, disclose any material effect of unmitigated risk on corporate profitability as well as strategies for preventing risks the company is exposed to.

**Shareholder voting decisions**

Section 242(1) of the CAMA requires the books containing the minutes of proceedings of any general meeting of a company to be kept at the registered office of the company and to be open to inspection by members without charge during business hours (subject to such reasonable restrictions as the company may by its articles or in general meeting impose, but so that no less than six hours in each day be allowed for inspection).

**Advertising of public offerings outside of the prospectus**

According to the ISA the advertisements on public offerings must be approved by the SEC prior to publication (Section 69(a) ISA, Rule 52(b) of the SEC Rules and Regulations).

**Material events**

The regulatory framework requires accurate, sufficiently clear and comprehensive and reasonably specific and timely disclosure of events that are material to the price or value of securities for public quoted companies.

According to the NSE Listing Rules companies listed at the NSE must immediately notify the Director-General of the NSE without delays of any facts and events that are material to price or value of the securities. Appendix III of the NSE Listing Rules includes the list of material events, but it is an open list as it indicates that the public companies must also provide any other information necessary to enable the shareholder to appraise the position of the company and to avoid the establishment of a false market in the shares of the company.

For public companies that are not listed at the NSE, no such obligation is clearly stated. In the discussion with the responsible department at the SEC, it was indicated that there is no monitoring by the SEC of the obligation to disclose material events for public companies not listed. The monitoring of compliance with the obligation for public companies listed is left to the NSE.

**Disclosure of the most significant risks of investing in the security**

It is required that the risk factors peculiar to the issuer should be stated in the prospectus including the following risks: risks associated with the business activities of the entity; sectoral risks, political risks, currency risks and environmental risks. Measures, if any, taken to address or mitigate the identified risk factors must be stated (Rule 56(3) of the SEC Rules and Regulations). Important relevant information about the issuer and its activities must be disclosed (Rule 56).

**Requirement to provide current information**

In addition to specific disclosure requirements, there is a general requirement to disclose either all material information or all information necessary to keep the disclosures made from being misleading. Rule 55 of the SEC Rules and Regulations makes parties liable for misleading statements or any omission of material fact in a prospectus.

The SEC has measures available to address concerns with the sufficiency, accuracy and timeliness of the required disclosures. They include review of the information by reporting accountant, certification by CEO and CFO and sanctions (Sections 80, 85, 86 ISA, Rules 40(b)(i)(iv)(h), 50(1(i)-(iii), 56(14)(c), administrative review on registration requirements, civil liability

for misleading statements in prospectus).

The ISA ensures that issuers and others involved in the issuing process are liable for the content of disclosures they make. The ISA and the SEC Rules and Regulations provide that issuers and others involved in the issuing process are liable for the content of disclosures they make (Sections 85, 86, 87 ISA and Rule 55(1)-(2)(c) on misleading statements in prospectus).

No prospectus is to be issued by or on behalf of a company or in relation to an intended company unless, on or before the date of its publication, a copy of the prospectus has been delivered to the SEC for registration, signed by every person who is named in it as a director of the company, or by his agent authorized in writing and having endorsed on it or attached to it (Section 80 (1) ISA).

There are no legal or regulatory provisions dealing with circumstances where disclosures related to trade secrets, similar proprietary information or other valid business purposes, such as incomplete negotiations, could be omitted or delayed. The ISA or the SEC Rules and Regulations do not grant any specific powers to the SEC in this regard, but the potential need for such derogations has arisen only rarely in the past.

ISA contains restrictions on and sanctions regarding the trading activities of persons with inside information. Section 111 of the ISA and Rule 110 of the SEC Rules and Regulations contain prohibition on insider dealings and manipulative and deceptive devices and contrivances.

#### Public offerings or listings by foreign issuers

There are only two foreign issuers listed at the NSE. All securities offered to the public by foreign issuers must be registered by the issuer or issuing house with the SEC. The registration statement for the distribution of the securities must be filed by the issuer or issuing house and must conform to the SEC Rules and Regulations for cross-border securities transactions (Rule 223).

#### Bond Issues Registered at the SEC 2009–August 2012

| Year | Types and Numbers        | Value<br>₦ million |
|------|--------------------------|--------------------|
| 2009 | 1 Corporate bond         | 13,165.00          |
|      | 3 State government bonds | 54,665.00          |
| 2010 | 6 Corporate bonds        | 77,290.00          |
|      | 5 State government bonds | 234,790.00         |
| 2011 | 10 Corporate bonds       | 83,138.06          |
|      | 5 State government bonds | 202,138.06         |
| 2012 | 2 State government bonds | 120,000.00         |

#### Equity Issues Registered at the SEC 2006–August 2012

| Year | Types and Numbers        | Value of Shares Offered<br>₦ million |
|------|--------------------------|--------------------------------------|
| 2009 | 1 Offer of subscription  | 3,300.50                             |
|      | 2 Rights                 | 27,522.00                            |
|      | 2 Private placements     | 417.25                               |
|      | <b>Total</b>             | <b>31,239.75</b>                     |
| 2010 | 5 Rights                 | 46,086.67                            |
|      | 7 Placements             | 74,252.33                            |
|      | <b>Total</b>             | <b>120,339.00</b>                    |
| 2011 | 7 Rights                 | 54,458.34                            |
|      | 10 Placements            | 161,366.54                           |
|      | 2 Placements to AMCON    | 854,015.37                           |
|      | 1 Preference share       | 8,435.18                             |
|      | <b>Total</b>             | <b>1,078,275.44</b>                  |
| 2012 | 5 Offers of subscription | 352,945,999                          |

|   |   |
|---|---|
| Assessment  | Fully Implemented   |
| Comments  | The disclosure standards for the Nigerian securities market are generally sound. However, the value of the disclosure requirements is entirely predicated upon the quality of the accounting and auditing conducted in practice in Nigeria and the enforcement of the relevant standards (see Principles 18 and 21). As indicated by several market participants interviewed, disclosure requirements are perceived to be more comprehensive and better monitored for banks than for other types of issuers. The NSE monitors ongoing disclosures relative to listed securities; the SEC does not have a program for monitoring and enforcing material event disclosures (see Principle 12).  |
| <b>Principle 17.</b> Holders of securities in a company should be treated in a fair and equitable manner. |   |
| Description   | <p><b>Rights and equitable treatment of shareholders</b></p> <p>The CAMA provides the basic framework for shareholder rights. The Nigerian legal and regulatory frameworks address the rights and equitable treatment of shareholders in connection with voting for election of directors. The CAMA contains the basic rights of shareholders in connection with the voting of directors (Part IX). The SEC Rules and Regulations (Rule 292(6)) contain the rules and basic rights for the election of directors.</p> <p>New provisions on protection of shareholder rights were introduced by the SEC Code of Corporate Governance that requires the Board to develop a written, clearly defined, formal and transparent procedure for the appointment of the Board of Directors. The Board should ensure that (22.1,22.2,22.3,22.5 SEC Code of Corporate Governance):</p> <ul style="list-style-type: none"> <li>• Shareholders' statutory and general rights, in particular their effective powers to appoint and remove directors, are protected at all times.</li> <li>• All shareholders are treated equally.</li> <li>• Minority shareholders are treated fairly at all times and adequately protected from abusive actions by controlling shareholders.</li> <li>• Shareholder representation on a Board should be proportionate to the size of shareholding.</li> </ul> <p>According to the SEC Code of Corporate Governance the question on whether a company is required to comply with or observe the Code or has complied with or observed the Code is, in the first instance, determined by the company's Board and shareholders and thereafter by the SEC. This creates certain ambiguity about the nature of the Code and the SEC's power to enforce it.</p> <p>The CAMA and the SEC Rules and Regulations establish that shareholders must be provided with any material information on corporate changes. Shareholders must be provided with any material information regarding bonus, profit-sharing and other other corporate actions where action is to be taken with respect to the acquisition or disposition of any operating property (Rules 292(7),(9) and (11) of the CAMA Rules and Regulations).</p> <p><b>Notice of shareholder meetings and voting decisions</b></p> <p>The CAMA contains the rules for the statutory, general and extraordinary meeting of shareholders. The notice required for all types of meeting is 21 days. The notice must contain the details indicated in Section 218(1) of the CAMA, i.e., mainly the nature of the business to be transacted in sufficient detail to enable the persons to decide whether to attend or not. Failure to give notice of any meeting to a person entitled to receive it invalidates the meeting.</p> <p>The SEC Code of Corporate Governance contains similar provisions. The notice should include copies of such documents, including annual reports and audited financial statements and other information, as will enable members to prepare adequately for the meeting. Procedures that enable beneficial owners to give proxies or voting instructions efficiently are in place. The CAMA provides the rules for the use of proxies (Section 230) while the SEC Rules and Regulations expand on these rules indicating what the proxy form must indicate and the need for</p> |

the proxy statement and proxy form to be furnished to the shareholder together with the notice of meeting and annual report 21 days before the date of the meeting in the case of the Annual General Meeting (AGM).

A copy of the proxy statement, proxy form and all other soliciting material in the form must be filed with the SEC. The use of proxies for mergers, acquisitions and combinations is regulated. There are provisions to deal with false statement on proxies (Rules 286, 287, 288).

Ownership registration (in the case of registered shares) and transfer of shares is contemplated in the CAMA. There is a fine of N200 to the company and every officer of the company who does not comply with the provisions of transfer and transmission of shares (Section 153 CAMA).

A company may offer or transfer its securities electronically; however when the investor elects to have a share certificate, the company must issue one.

Every registrar must keep a manual and/or electronic register of members of client companies with adequate back-ups which must be stored in a safe place outside the premises of the registrar (Rules 98, 194–198 of the SEC Rules and Regulations).

The receipt of dividends and other distributions, when, as, and if declared is a function of the registrar

The registrar must keep the register of the members of a company and make the appropriate changes in the register. The registrar must also prepare and dispatch dividend/interest warrants. A dividend declared must be paid by the issuance of a check or transfer of funds to the registrar no later than seven working days after the AGM where the dividend was declared (Rules 193(1)(iv) and 204 of the SEC Rules and Regulations).

The regulation of transactions involving a takeover bid indicates that where any person acquires shares, whether by a series of transactions over a period of time or not, which taken together with shares held or acquired by a person acting in concert with him carry 30 percent or more of the voting rights of the company, or together with a person acting in concert with him, holds not less than 30 percent but not more than 50 percent of the voting rights and such person or any person acting in concert with him acquires additional shares which increase his percentage of the voting right, such person must make a takeover offer to the holder of any class of equity share capital in which such person or any person acting in concert with him holds shares.

It is clearly stated that all shareholders of the same class of an offeree company must be treated similarly by an offeror.

An authority to proceed with the takeover bid needs to be granted by the SEC that must be informed at the date of the takeover bid (Section 134 ISA).

There is no antitrust or competition agency in Nigeria. When deciding whether or not to grant an authority to proceed with a takeover bid, the SEC must have regard to the likely effect of the takeover bid on the economy of Nigeria and on the policy of the federal government with respect to manpower and development. If the SEC is satisfied that none of these matters are adversely affected, it must grant an authority to proceed with the proposed takeover bid.

If a director makes a takeover bid without the approval of the corporation, he/she commits an offence and is liable on conviction to a fine of not less than ₦100,000 or to imprisonment for a term not exceeding twelve months or to both such fine and imprisonment.

Where a bid under a takeover bid is for less than all the shares of any class in the offeree company and a greater number of shares than the offeror is bound or willing to take up and pay is deposited pursuant to the bid, the offeror must take up the shares pro rata according to the number of shares deposited by each shareholder.

The SEC must place on the file of the offeree company any bid or amendment to it (Section 131–150 ISA, Rule 235 of the SEC Rules and Regulations).

#### **Other change of control transactions**

Section 118(1) of the ISA requires that every merger, acquisition or business combination between or among companies must be subject to the review and approval of the SEC. The following table indicates the number of change of control transactions that have taken place in Nigeria from January 2009 to August 2012.

| <b>Type of transaction</b>    | <b>2009</b> | <b>2010</b> | <b>2011</b> | <b>2012<br/>(January-August)</b> |
|-------------------------------|-------------|-------------|-------------|----------------------------------|
| Mergers                       | 1           | 3           | 5           | 2                                |
| Acquisition/Management Buyout | 11          | 6           | 14          | 4                                |
| Restructuring                 | 0           | 4           | 18          | 5                                |
| Takeover                      | 0           | 0           | 0           | 1                                |

The SEC is empowered to hold a company, its directors and senior management liable for contraventions of the ISA provision with respect to registration of securities. The issuers registered with the SEC are responsible for filing with the SEC on quarterly, half yearly and annual basis their financial information as prescribed by the SEC. The CEO and CFO must provide a certification that the annual report does not contain any untrue statement of a material fact or does not omit to state a material fact, which would make the statement misleading. Any contravention of the obligation of the company to present financial reports as mentioned as the result of any neglect on the part of a director, manager, secretary or other similar officer, servant or agent of the company or any person purporting to act in any such capacity or as a result of a director, manager, secretary or other similar officer, servant or agent of the company to act in such capacity knowingly or willfully authorizing the contravention, the individual in question is liable to the same extent as the issuer. The SEC is authorized to administratively apply penalties prescribed for such violations.

Provisions on a bankruptcy of a company are included in the CAMA.

#### **Shareholder voting decisions**

Full disclosure of all information material to an investment or voting decision is required in connection with shareholder voting decisions.

With respect to transactions regarding control changes shareholders affected by the proposal are given a reasonable time in which to consider the proposal. In case of a takeover bid shareholders are given up to 21 days in the case the bid is for less than all the shares of the offeree company. In the case a bid under a takeover bid is for all or less than all the shares of any class in the offeree company the shareholder may withdraw the shares deposited pursuant to the bid at any time within 10 days after the date of the take-over bid (Section 143–146 ISA).

Shareholders are supplied with adequate information to enable them to assess the merits of the proposal. The requirement as to the bid under a takeover bid are comprehensive and include the terms on which those shares are proposed to be acquired and set out how and by what date the obligations of the offeror are to be satisfied. It is an offence and each director is liable, if default is made in complying with the provision regarding the information that must be provided to the shareholder in a takeover bid. The sanction for not complying that could be imposed to each director is a fine of not less than ₦100,000 or imprisonment for a term not exceeding 12 months or both such fine and imprisonment (Section 136 and 138 ISA, Rule 236 of the SEC Rules and Regulations).

Shareholders are given reasonable and equitable opportunities to participate in any benefits accruing to the shareholders under the proposal.

Shareholders must be given fair and equitable treatment in relation to the proposal. Section 146 of the ISA on acquisition of shares of dissenting shareholders includes provisions on the treatment of outstanding shares, which refers to shares in respect of which a takeover bid was made but has not been accepted. A dissenting offeree means a person who is, or is entitled to be registered as a holder of outstanding shares. The dissenting offeree has the right to be informed of the choice which he is required to make to either transfer his shares to the offeror on the terms on which the offeror acquired the shares from an offeree that accepted the takeover bid or to demand payment of the fair value of the shares. The offeror may, within twenty days after he had paid to the offerees apply to the court to fix the fair value of shares of the dissenting offeree. There are no specific regulatory requirements on the calculation of fair value.

#### **Requirement for the directors of the offeree company**

The directors of an offeree company must send a directors' circular to each shareholder of the offeree company and to the SEC at least seven days before the date on which the takeover bid is to take effect. They may recommend that no shares be tendered pursuant to the takeover bid until the directors' circular is sent. When the director of the offeree company is of the opinion that the takeover bid is not advantageous to the shareholders, or disagrees with any statement in a directors' circular he is entitled to indicate his opinion or disagreement in the directors' circular. The directors' circular must include particulars of any payment made to an officer or former officer of an offeree company by the way or compensation for loss of his office or as consideration for or in connection with his retirement from any office (Section 140 ISA.)

#### **Notification of large shareholdings**

Information about the identity and holdings of the most important shareholders is required to be included in the public offering and listing particulars documents. More specifically, Rule 56(1)(x) of the SEC Rules and Regulations requires information on the principal shareholders to be included in a prospectus. The concept of a principal shareholder is not defined in the SEC Rules and Regulations. The rules are more specific for cross-border offers and require that the names and the percentage of shares owned by the company's major shareholders (i.e., the beneficial owners of 5 percent or more of each class of the company's voting securities) need to be disclosed in the prospectus as of the most recent practicable date, or an appropriate negative statement needs to be included if there are no major shareholders. Any significant change in the percentage ownership held by any major shareholder during the past three years also needs to be disclosed (Rule 225(8) of the SEC Rules and Regulations).

Every registrar needs to file with the SEC information on beneficial owners of 5 percent or more of the company's shares and any subsequent transactions by the holder. The information must be filed within five days of the change in ownership (Rule 109A). The information is available for review at the SEC, but in practice it is not easily accessible. The registrars also file this information on a quarterly basis, and the SEC monitors the large shareholdings from those returns.

In the case of listed companies, as required by the listing rules a statement as at the end of the financial year showing the interest of each director in the share capital of the company must be published. The statement must include, by way of a note, changes in the directors' interests occurred between the end of the financial year and a date not more than one month prior to the date of notice of the AGM, or if there has been no such change, disclosure of that fact.

Listed companies must also provide the NSE a statement showing particulars as at a date not more than one month prior to the date of notice of the AGM of an interest of any person, other than a director, who holds 5 percent or more in the equity of the company and the actual amount so held or, where appropriate, a negative statement.

|   |   |
|---|---|
|   | <p>It is not clear how effectively the SEC and the NSE have enforced compliance with the above requirements.</p> <p>There are no specific requirements on the application of the disclosure requirements to two or more persons acting in concert.</p> <p><b>Filing of notice by directors and other insiders upon sale or purchase of their shares in the company</b></p> <p>With respect to holdings of voting securities by directors and senior management the information about the beneficial ownership interest and material changes in beneficial ownership in a company is required to be disclosed in a timely manner.</p> <p>Directors and other insiders of public companies must notify the SEC of the sale of their shares in the company or any purchase of shares in the company not later than 48 hours after such activity. Such information is available to the public.</p> <p><b>Cross-border matters</b></p> <p>The public offerings or listings by foreign issuers are not significant in Nigeria; however the rules for cross-border listings require disclosure in foreign issuers' offering and listing particulars documents of any governance provisions or information relating to the foreign issuer's jurisdiction that may materially affect the fair and equitable treatment of shareholders (Rule 225 of the SEC Rules and Regulations on contents of prospectus for offerings).</p>   |
| Assessment  | Partly Implemented  |
| Comments  | <p>The legal requirements for the disclosure of major shareholdings are fairly appropriate, but in practice the investors do not have sufficient access to the disclosures since they are not electronically available. The SEC should, in cooperation with the NSE, seek to improve access to this important information and ensure that the disclosure obligations are sufficiently enforced. The same applies to the disclosures made by company insiders.</p>   |
| <b>Principle 18.</b> Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality. |   |
| Description   | <p><b>Requirement to include audited financial statements in public offering and listing documents</b></p> <p>In Nigeria five year historical financial information including the accountant's report, accounting policies, balance sheets, profit and loss accounts, cash flow statements and notes to the accounts is required to be included in the prospectus. If the company has existed for less than five years, audited historical financial information for the number of years in existence or an audited statement of affairs for a new company has to be provided.</p> <p><b>Requirement to include audited financial statements in annual reports</b></p> <p>Every public company whose securities are required to be registered must file with the SEC, on a periodic or annual basis and in a specified format, its audited financial statements and other returns as may be prescribed by the SEC from time to time.</p> <p>The audited financial statements, whether interim or final, are required to include a balance sheet, income statement or profit and loss account, statement of changes in equity, statement of cash flows, as well as notes, statements and explanatory materials and other documents as required under CAMA and any other relevant accounting standards.</p> <p>Since January 2012, financial statements required in public offering and listing documents in Nigeria and publicly available annual reports are required to be prepared in accordance with IFRS.</p> |

As such, the IFRS as accounting standards require financial statements to be comprehensive, to be designed to serve the needs of investors, to reflect consistent application, and to be comparable if more than one accounting period is presented. The transition to the IFRS happens in such a manner that the closing balances of December 2010 need to be converted to IFRS-based figures which then become the opening balances as at January 1, 2011 for IFRS-based financial statements as at December 31, 2011. This provides opening balances for January 1, 2012 which is the first year for full IFRS financial statements (with 2011 as the comparative year).

#### **Establishment of the FRC**

Since 2011, there has been a major change in the setting of accounting standards in Nigeria. The new organization responsible for the establishment and timely updating of accounting standards is the Financial Reporting Council (FRC). It has replaced the Nigerian Accounting Standards Board (NSAB). The NSAB Act of 2003 was repealed and the FRC Act establishing the FRC came into force in 2011. The FRC is responsible for, among other things, developing and publishing accounting and financial reporting standards to be observed in the preparation of financial statements of public entities in Nigeria. The FRC may issue rules and guidelines for the purpose of implementing auditing and accounting standards.

The Nigerian regulatory framework provides that the FRC is the organization responsible for the establishment and timely interpretation of accounting standards. The FRC has determined that the accounting standards to be used in Nigeria since January 1, 2012 are the IFRS. The IFRS are applicable to "public interest entities" which means governments, government organizations, quoted and unquoted companies and all other organizations which are required by law to file returns with regulatory authorities (FRC definitions).

Unaudited financial statements used in quarterly reports of issuers registered with the SEC are also required to be presented in accordance with the IFRS since January 1, 2012.

Some of the FRC's main objectives are to:

- Protect the interest of investors and other stakeholders;
- Give guidance on issues relating to financial reporting and corporate governance to professional, institutional and regulatory bodies in Nigeria;
- Ensure good corporate governance practices in the public and private sectors of the Nigerian economy;
- Ensure accuracy and reliability of financial reports and corporate disclosures, pursuant to the various laws and regulations currently in existence in Nigeria;
- Harmonize activities of relevant professional and regulatory bodies as relating to corporate governance and financial reporting;
- Promote the highest standards among auditors and other professionals engaged in the financial reporting process;
- Enhance the credibility of financial reporting; and
- Improve the quality of accountancy and audit services as well as actuarial, valuation and corporate governance standards.

The powers and functions of the FRC as the new standard setter, regulator and supervisor are comprehensive. They include to:

- Develop and publish accounting and financial reporting standards to be observed in the preparation of financial statements of public interest entities;
- Review, promote and enforce compliance with the accounting and financial reporting standards adopted by the FRC;
- Receive notices of non-compliance with approved standards from preparers, users, other third parties or auditors of financial statements;
- Receive copies of annual reports and financial statements of public interest entities from preparers within 60 days of the approval of the Board;

|  |   |
|--|---|
|  | <ul style="list-style-type: none"> <li>• Advise the federal government on matters relating to accounting and financial reporting standards;</li> <li>• Maintain a register of professional accountants and other professionals engaged in the financial reporting process;</li> <li>• Monitor compliance with the reporting requirements specified in the adopted code of corporate governance;</li> <li>• Promote compliance with the adopted standards issued by the International Federation of Accountants and International Accounting Standards Board;</li> <li>• Monitor and promote education, research and training in the fields of accounting, auditing, financial reporting and corporate governance;</li> <li>• Conduct practice reviews of registered professionals;</li> <li>• Review financial statements and reports of public interest entities<sup>2</sup>;</li> <li>• Enforce compliance with the FRC Act and the FRC rules on registered professionals and the affected public interest entities;</li> <li>• Establish such systems and schemes or engage in any relevant activity, either alone or in conjunction with any other organization or agency, whether local or international, for the discharge of its functions ;</li> <li>• Receive copies of all qualified reports together with detailed explanations for such qualifications from auditors of the financial statements within a period of 30 days from the date of such qualification (such reports must not be announced to the public until all accounting issues relating to the reports are resolved by the Council);</li> <li>• Adopt and keep up-to-date accounting and financial reporting standards, and ensure consistency between standards issued and the International Financial Reporting Standards;</li> <li>• Specify, in the accounting and financial reporting standards, the minimum requirements for recognition, measurement, presentation and disclosure in annual financial statements, group annual financial statements or other financial reports which every public interest entity must comply with, in the preparation of financial statements and reports;</li> <li>• Develop or adopt and keep up-to-date auditing standards issued by relevant professional bodies and ensure consistency between the standards issued and the auditing standards and pronouncements of the International Auditing and Assurance Standards Board; and</li> <li>• Perform such other functions which in the opinion of the Board are necessary or expedient to ensure the efficient performance of the functions of the Council.</li> </ul> <p>The FRC has the powers given by the FRC Act to enforce and approve enforcement of compliance with accounting, auditing, corporate governance and financial reporting standards in Nigeria. However, since it was established only recently, it has not yet fully established itself as the enforcer of accounting standards.</p> <p>According to the FRC Act, the FRC’s board members, which include the SEC and the NSE, will be:</p> <ul style="list-style-type: none"> <li>• Association of National Accountants of Nigeria;</li> <li>• Institute of Chartered Accountants of Nigeria;</li> <li>• Office of the Accountant General of the Federation;</li> <li>• Office of the Auditor General for the Federation;</li> </ul> |
|--|---|

<sup>2</sup> Significant public interest entities are government business entities, all entities that have their equities or debt instruments listed and traded in a public market (a domestic or foreign stock exchange or an OTC market, including local and regional market), and such other organizations, though unquoted, required by law to file returns with regulatory authorities. Examples of entities meeting these criteria include financial and other credit institutions and insurance companies. Other public interest entities are those entities, other than listed entities (unquoted, private companies), which are of significant public interest because of their nature of business, size, number of employees or corporate status which require wide range of stakeholders. Examples of entities meeting these criteria are large not for profit entities such as charities and pension funds. They may also include publicly owned entities and other entities where there is a potentially significant effect on financial stability.

- Central Bank of Nigeria;
- Chartered Institute of Stockbrokers;
- Chartered Institute of Taxation of Nigeria;
- Corporate Affairs Commission;
- Federal Inland Revenue Service;
- Federal Ministry of Trades and Investment;
- Federal Ministry of Finance;
- Nigerian Accounting Association;
- Nigerian Association of Chambers of Commerce, Industries, Mines and Agriculture;
- Nigerian Deposit Insurance Corporation;
- Nigerian Institute of Estate Surveyors and Valuers;
- Securities and Exchange Commission;
- National Insurance Commission;
- Nigerian Stock Exchange; and
- National Pension Commission.

As of the date of the assessment the FRC Board had not yet been nominated. Once constituted the Board should meet eight times per year.

#### **Register of professionals**

A professional, for the purpose of registration with the FRC, refers to any person whose education and training allow for his judgment to be relied upon and possesses a certification issued by a recognized professional body or association.

The FRC has published a list of 89 recognized professional bodies which includes:

- Institute of Chartered Accountants of Nigeria (ICAN);
- Association of National Accountants of Nigeria (ANAN);
- Institute of Certified Public Accountants of Nigeria;
- Chartered Institute of Cost & Management Accountants of Nigeria and
- Institute of Company & Commercial Accountants of Nigeria.

With the issuance of the FRC Act, the two professional accountancy bodies operating in Nigeria, ICAN and ANAN (Acts of 1965 and 1993, respectively) continue to exist. They are now members of the Board of the FRC. However their previous role as self-regulators of the profession has now been given to the FRC as a public regulator.

There is no direct relationship between the FRC and the International Accounting Standards Board (IASB). The FRC does not receive financial or technical assistance from the IASB. According to the FRC any conflict between a Nigerian accounting standard (the Statement of Accounting Standard) and an International Accounting Standard/International Financial Reporting Standard should be resolved in favor of the Nigerian standard. This is because the pronouncements of each national accounting standard-setting body determine accounting principles and practices to be used in its country.

#### **Openness and transparency of FRC's processes**

On the basis of the FRC Act and a discussion with the FRC personnel, the FRC has the regulatory framework in place to be considered independent. The standard setting and interpretation process is designed to be undertaken in cooperation with all the relevant stakeholders, including the SEC which is a member of the FRC Board. However the system for enforcing compliance with accounting standards does not yet seem to be fully operational.

The FRC has a Directorate of Inspection and Monitoring. This Directorate is in charge of monitoring compliance with auditing, accounting, actuarial and valuation standards and guidelines reviewed

|  |  |
|--|--|
|  | <p>and adopted by the FRC and recommending through the Technical and Oversight Committee any necessary sanctions for the FRC's approval and implementing approved sanctions and fines. The FRC has currently a staff of 262 people. The FRC is receiving technical assistance and cooperation from the United Kingdom's Financial Reporting Council. The FRC is self-funded with levies from the companies.</p> <p><b>Public offerings or listings by foreign issuers</b></p> <p>Public offerings or listings by foreign issuers are not significant in Nigeria. However the SEC permits the use of high quality, internationally acceptable accounting standards by foreign companies that wish to list or offer securities in the country (Rule 225(9) of the SEC Rules and Regulations).</p>  |
| Assessment   | Broadly Implemented  |
| Comments   | <p>The approval of the FRC Act and the transition to the IFRS imposes challenges to the financial market participants. It will be necessary to monitor the progress of the FRC in monitoring the compliance with the IFRS. Although the FRC is a new regulator it has already given some indications of the way it will act, for example it recently challenged the ICAN's own financial statements. It also builds on the operations of the NASB, and has therefore been able to make progress in setting up its administration and internal procedures even though its Board has not yet been nominated.</p> <p>Interviews conducted with market participants suggest a lack of adequate capacity to prepare IFRS-based financial statements.</p> <p>A knowledge gap on IFRS-based financial reporting is a significant challenge faced by the accountancy profession in Nigeria. In discussions with market participants, accountants and auditors, the assessors were told that the market might not have adequate resources or ability to prepare IFRS-based financial statements. It is possible therefore that in these cases the auditors might either prepare or provide substantial assistance with the preparation of such financial statements. This however raises a significant independence issue.</p>  |
| <b>Principles for Auditors, Credit Ratings Agencies, and Other Information Service Providers</b> |  |
| <b>Principle 19.</b> Auditors should be subject to adequate levels of oversight.                 |  |
| Description  | <p><b>Nigerian regulatory system for overseeing quality of auditing</b></p> <p>With the enactment of the FRC Act the Nigerian regulatory system provides a framework for overseeing the quality and implementation of auditing, independence and ethical standards, including the quality control environments in which auditors operate.</p> <p>Auditors are required to be qualified and competent pursuant to minimum requirements before being licensed to perform audits, and to maintain professional competency. Only accountants duly recognized and entitled to practice as such under the laws of Nigeria are recognized by the SEC. Accountants barred by the SEC are not recognized by it and are barred from acting as such in connection with any public offering.</p> <p>An auditor that carries on the business of auditing a public company and is not registered by the SEC is liable to a penalty of not less than ₦1,000,000 and further penalty of ₦25,000 per day for the period the violation continues. (Section 65 of the ISA)</p> <p><b>Regulation of accountants and auditors</b></p> <p><i>Reporting accountants</i></p> <p>There are 150 reporting accountants registered by the SEC. Reporting accountants (Rule 206) have to review the issuer's audited accounts for which they must review audit working papers, discuss with the company's management and auditors all significant changes, and ascertain that</p> |

the accounting policies utilized are in compliance with applicable accounting standards.

The reporting accountant's report is addressed jointly to the directors of the issuer and the issuing house and disclosed in the prospectus. If the reporting accountant knowingly fails to point out any discrepancies in the work done by the auditor, he is liable for any loss occasioned thereby and may be reported to his professional body for disciplinary actions.

#### *Auditors*

No person is allowed to carry on the business of auditing of a public company unless that person is registered by the SEC (Section 62 ISA, SEC Code of Corporate Governance).

In the case of managers of CIS the SEC needs to be satisfied of the competence of the auditor in respect of matters which they would be concerned in relation to the CIS and the probity of the external auditor.

#### **Oversight by the SEC and NSE**

The SEC in 2007 established the Financial Standards and Corporate Governance Department to review financial statements of all the issuers registered with the SEC for ensuring compliance with the accounting standards and disclosure requirements. However, this initiative remains at a nascent stage. The officials responsible for monitoring and related activities are developing the knowledge on practical aspects of applying the IFRS. Enforcement actions taken by the SEC include penalizing a number of companies for delay in the filing of financial statements.

The NSE has started delisting issuers for lack of compliance with the listing requirements. The assessors were provided with a list of the companies delisted by the NSE. From 2002 to August 2012, 47 companies were delisted, out of which only three companies between 2002 and 2007. In 2008, 18 companies were delisted from the NSE. So far in 2012, 13 companies have been delisted.

#### **Oversight by the FRC**

After the approval of the FRC Act, the FRC is responsible for, among other things, developing and publishing accounting and financial reporting standards to be observed in the preparation of financial statements of public entities in Nigeria. The FRC is also currently establishing the process for performing regular reviews of audit procedures and practices of firms that audit financial statements of issuers registered with the SEC. The processes for regular assessments by the FRC on whether the external auditor is and remains independent, both in fact and in appearance, of the enterprises that it audits are being established.

The FRC is an oversight body that operates in the public interest, has an appropriate membership, and an adequate charter of responsibilities and powers. It has adequate funding, such that the oversight responsibilities are carried out in a manner independent of the auditing profession.

According to the FRC Act, a professional accountant in the exercise of his audit function must carry out his function in full independence and must not act in any manner contrary to the Code of Conduct and Ethics that may be made by the FRC or under any enactment in force or engage in any activity likely to impair his independence as a professional. Where a professional accountant considers that he may have a conflict of interest in relation to an entity for which he has been engaged as a professional accountant, he must disclose to the entity and the FRC the nature of the conflict of interest in order to enable the entity to determine the extent of the conflict and to decide whether or not to continue retaining the services of the professional accountant (FRC Act Sections 46 and 47).

The FRC is not yet conducting any reviews on a recurring basis that would be designed to

|  |  |
|--|--|
|  | <p>determine the extent to which audit firms have and adhere to adequate quality control policies and procedures that address all significant aspects of auditing. The FRC is expected to conduct reviews of audit firms and auditors every three years.</p> <p><b>Remedial measures</b></p> <p>The FRC can initiate and carry out disciplinary proceedings to impose sanctions on auditors and audit firms, as appropriate. However, due to the recent creation of the FRC, this authority has not yet been used.</p> <p>The FRC has a Directorate of Corporate Governance. Among the objectives of the Directorate are to promote sound financial reporting and accountability based on true and fair financial statements duly audited by competent independent auditors and to ensure that audit committees of public interest entities keep under review the scope of the audit and its cost effectiveness and the independence and objectivity of the auditors</p>   |
| Assessment   | Partly Implemented   |
| Comments   | The auditor oversight process has just started without any concrete results yet. It is necessary to continue to develop IFRS technical capacity in the SEC. Immediate steps should be taken to prepare a team of IFRS experts at the SEC. These experts should be able to effectively carry out activities at the SEC, in collaboration with the FRC, with regard to ensuring IFRS compliance by the issuers registered with the SEC. Similar IFRS technical capacity building is necessary at the NSE.  |
| <b>Principle 20.</b> Auditors should be independent of the issuing entity that they audit. |  |
| Description  | <p><b>Standards for the independence of external auditors</b></p> <p>The CAMA indicates on the matter of appointment and removal of auditors that none of the following persons is qualified for appointment as an auditor of a company:</p> <ul style="list-style-type: none"> <li>• an officer or servant of the company;</li> <li>• a person who is a partner of or in the employment of the company; and</li> <li>• a body corporate.<sup>3</sup></li> </ul> <p>Any report by accountants required by the ISA must be made by accountants qualified under the ISA for appointment as auditors of a company.</p> <p>The SEC Code of Corporate Governance states that, in addition to its statutory functions, the audit committee has the following responsibilities regarding auditor independence:</p> <ul style="list-style-type: none"> <li>• Assist in the oversight of the integrity of the company's financial statements, compliance with the legal and other regulatory requirements, and assessment of qualifications and independence of the external auditor;</li> <li>• Review the independence of the external auditors and ensure that where non-audit services are provided by the external auditors there is no conflict of interest; and</li> <li>• Preserve auditor independence, by setting clear hiring policies for employees or former employees of independent auditors.</li> </ul> <p>In order to safeguard the integrity of the external audit process and guarantee the independence of the external auditors, companies should rotate both the audit firms and audit partners. Companies should require external audit firms to rotate audit partners assigned to undertake the external audit of the company from time to time to guarantee independence. An external audit firm should be retained for no longer than ten years continuously. External audit firms disengaged after</p> |

<sup>3</sup> In practice audit firms are however appointed as auditors.

|            |  |
|------------|--|
|            | <p>continuous services to a company for ten years may be reappointed seven years after their disengagement.</p> <p>Independence of auditors is required for CIS. A manager in consultation with the trustee must appoint an auditor registered by the SEC for the purpose of auditing the whole of the business of the scheme administered by it. No director or employee of a manager, trustee or custodian and no firm of which any such director or employee is a member may be appointed as an auditor of a scheme (Section 184(1)-(2) ISA).</p> <p>The FRC has as one of its objectives to promote the highest standards among auditors and other professionals engaged in the financial reporting process.</p> <p>Auditors when auditing public interest entities as defined in the FRC Act must conduct the audit following International Standards on Auditing and its independence rules.</p> <p>Requirements for the auditors to establish and maintain internal systems, governance arrangements and processes for monitoring, identifying and addressing threats to independence, including the rotation of auditors, and ensuring compliance with the standards have not yet been issued by the FRC.</p> <p>From the perspective of public companies, the external auditor is required to be independent in both fact and appearance of the entity being audited. The FRC Act provides for the need of the auditor to be independent.</p> <p>Every public company must establish an Audit Committee with written terms of reference. The Committee must be independent in carrying out its terms of reference. The Audit Committee must maintain records of attendance and deliberations of its meetings and interactions. The Audit Committee must review the company's financial statements prior to approval by the Board of the company and present the report at the Annual General Meeting. The Audit Committee must also oversee the process of selection and appointment of the external auditor and assess his independence (SEC Code of Corporate Governance).</p> <p><b>Disclosure of the resignation, removal or replacement of an external auditor</b></p> <p>Every company must at each AGM appoint an auditor to audit the financial statements of the company, and to hold office from the conclusion of that until the conclusion of the next AGM.</p> <p>The directors of a company, within one week of an AGM where no auditors were appointed or re-appointed must give notice of that fact to the SEC, and if the company fails to give notice, the company and every officer of the company who is in default is guilty of an offence and liable of N100 for every day during which the default continues (Section 357(2) CAMA).</p> <p>At any AGM at which directors are elected and/or financial statements are presented, information on whether the auditor has been changed and on whether the reason for the change is a result of a disagreement between the auditor and issuer needs to be disclosed.</p> <p>Adequate mechanism for enforcing compliance with the auditor independence standards to stipulate remedial measures for problems detected, to initiate and carry out disciplinary proceedings, to impose sanctions on auditors and audit firms as appropriate, or to refuse to accept, or require revision of, audit reports, or to impose sanctions for lack of independence are now available to the FRC with the enactment of the FRC Act. However these mechanisms are yet to be developed and implemented.</p> |
| Assessment | Partly Implemented   |
| Comments   | Although the adoption of the FRC Act and the establishment of the FRC as the new regulator are positive steps taken, auditor independence is not yet adequately monitored by the new regulator.  |

|  |  |
|--|--|
| <b>Principle 21.</b> Audit standards should be of a high and internationally acceptable quality.   |  |
| Description  | <p>As explained in Principle 18 the new setter of auditing standards in Nigeria is the FRC. The FRC has established that the audit standards that must be followed by auditors that conduct audits of public companies' financial statements in Nigeria since January 1, 2012 are the International Standards on Auditing (IAS).</p> <p>The functions of the FRC's Directorate of Auditing Practices Standards include:</p> <ul style="list-style-type: none"> <li>• develop or liaise with relevant professional bodies on auditing and ethical standards set by the FRC;</li> <li>• promote auditing standards which set out the basic principles and essential procedures with which external auditors in Nigeria are required to comply;</li> <li>• issue guidance on the application of auditing standards in particular circumstances and industries and timely guidance on new and emerging issues;</li> <li>• establish standards and related guidance for accountants providing assurance services;</li> <li>• encourage establishment of ethical standards in relation to the independence, objectivity and integrity of external auditors and those providing assurance services;</li> <li>• play appropriate role in the development of regulations and accounting standards which affect the conduct of auditing and assurance services, both domestically and internationally; collaborate with relevant professional bodies to advance public understanding of the roles and responsibilities of external auditors and the providers of assurance services including the sponsorship of research; and</li> <li>• perform such other duties which in the opinion of the Board of the FRC are necessary or expedient to ensure the efficient performance of external auditors.</li> </ul> <p><b>Mechanism for enforcing compliance with auditing standards.</b></p> <p>The FRC has a Directorate of Inspection and Monitoring which:</p> <ul style="list-style-type: none"> <li>• monitors compliance with auditing, accounting, actuarial and valuation standards and guidelines reviewed and adopted by the FRC;</li> <li>• recommends through the Technical and Oversight Committee sanctions as may be necessary for the FRC's approval; and</li> <li>• implement sanctions and fines as approved by the FRC.</li> </ul> <p>The FRC was established in 2011. At the moment just one regulatory decision from August 2012 in the matter of the audited financial statements of one insurance company is available at the FRC's website. In the discussions with the FRC personnel it was confirmed that mechanisms to enforce compliance with the auditing standards are being developed by the FRC.</p> |
| Assessment   | Broadly Implemented  |
| Comments   | The FRC as the standard setter of the auditing standards in Nigeria is at an incipient stage. Its Board has not yet been appointed.  |
| <b>Principle 22.</b> Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision. |  |
| Description  | <p><b>Registration</b></p> <p>There is no definition of credit rating or credit rating agency in the Nigerian legislative/regulatory framework. Since the use of credit ratings provided by credit rating agencies registered in Nigeria is mandatory in certain cases, the entities that provide such ratings would however be identified and would become subject to the requirement to register with the SEC. Currently there are five registered credit rating agencies in Nigeria.</p> <p>The provision of a rating report by a registered rating agency is mandatory at least in the following</p>   |

|  |  |
|--|--|
|  | <p>cases:</p> <ul style="list-style-type: none"> <li>• application for registration of a debt instrument with the SEC, including a bond or other debt security issued by a state/local government or other government agency (Rules 40 and 307 of the SEC Rules and Regulations);</li> <li>• as part of the information included in the prospectus for a debt instrument (Rule 56);</li> <li>• for a filing with the SEC on a real estate investment scheme every two years (Rule 280A);</li> <li>• in order for a CIS to be allowed to invest in unlisted securities, the company needs to be rated investment grade by a reputable<sup>4</sup>/SEC registered rating agency (Rule 281A(4)); and</li> <li>• according to the Pension Reform Act 2004, every pension fund administrator is required to have due regard to the risk rating of the instruments undertaken by a risk rating company registered under the ISA.</li> </ul> <p>According to the SEC staff, credit rating agencies have gained importance in Nigeria only recently when the state bonds became more common. A credit rating is important also in the cases where the repayments of the bond are backed by an Irrevocable Standing Payment Order (ISPO),<sup>5</sup> because the credit rating assesses the adequacy and quality of the revenue created internally in the state. With different internal revenue levels in various states, their credit ratings can be very different.</p> <p>The registration requirements for credit rating agencies are set out in Rule 38 of the SEC Rules and Regulations. The requirements include a list of specific information to be provided, but also provide the possibility for the SEC to require the applicant to file any other document or information.</p> <p>Rule 38(1) of the SEC Rules and Regulations was amended in September 2011 to allow the SEC to consider on a case by case basis granting a foreign credit rating agency a registration exemption certificate to enable it to participate in any transaction in the capital market, provided such credit rating agency is validly registered in a jurisdiction that has established regulatory and supervisory frameworks in accordance with the standards set out by IOSCO. Evidence of such registration, including such additional supporting documents as may be specified by the SEC from time to time, must be filed along with the application for the registration exemption certificate. No such exemptions have yet been given. In addition, it appears that the wording of the above mentioned Rules 40, 56 and 307 were not amended at the same time, which would seem to make it legally difficult to use ratings provided by foreign credit rating agencies in Nigeria.</p> <p>Rule 38(2) of the SEC Rules and Regulations includes requirements on the information that a rating agency in Nigeria affiliated to a foreign rating company should supply in its application for registration, however no such companies currently exist.</p> <p>The SEC is required to decide on whether it grants the registration within 60 days after the filing of an application, providing reasons for its decision (Rule 29(3) and (4) of the SEC Rules and Regulations). The SEC may also by order suspend or cancel a certificate of registration of a CRA (Section 38(4)-(6) ISA).</p> <p><b>Ongoing supervision</b></p> <p>Under Section 13(t) of the ISA, the SEC can require any person to provide such information as it may consider necessary for the efficient discharge of its functions, which provides it with the ability to obtain all information about a regulated CRA that it deems necessary for adequate supervision.</p> <p>The SEC monitors the activities of CRAs through the quarterly reports (SEC/QR/11) they are</p> |
|--|--|

<sup>4</sup> The term reputable does not appear to be defined in the regulatory framework.

<sup>5</sup> An ISPO allows the Office of the Accountant General of the Federation to deduct funds from the State's gross allocation on a monthly basis for the repayment of the loan.

required to submit. In addition to providing standard information required from all registered entities (e.g., change of directors, partners and registered personnel, number of board meetings, amount of capital and information on any litigations), the CRAs are required to provide information on each rating they provided during the quarter (including name of the client, type of issue, rating, and whether the rating was solicited/unsolicited). They also need to inform the SEC about any changes in their rating methodology and the reasons for those changes. Finally, they are required to provide information on employees' trading in the securities of any of the entities rated/to be rated by the rating agency.

According to Section 45 of the ISA, the SEC is required to conduct routine and special inspections and investigations of Capital Market Operators, including CRAs. It is also required to order a special examination or investigation of the books and affairs of a Capital Market Operator in cases stipulated in Section 47 of the ISA (e.g., public interest, contravention of the ISA, application by a director or shareholder of the CMO). So far the SEC has not conducted any on-site inspections in CRAs.

Under the general sanctioning powers of the SEC (Section 303 ISA), any person (including a CRA) who violates or contributes in the violation of the provisions of the ISA or of any rule and regulation made thereunder is liable to a penalty of not less than ₦100,000 and a further sum of ₦5,000 per day for every day that the violation continues. The SEC may in addition to any penalty direct any person who has contravened any of the provisions of the ISA or any regulation made thereunder, to compensate any person who may have suffered any direct loss as a result of the contravention. In appropriate cases, the SEC may also direct any direct benefit or advantage received or receivable by the contravening person to the victim.

**Oversight requirements: quality and integrity**

An application for registration as a CRA has to be accompanied by details of its rating criteria, methodology and principles (Rule 38(3)(ix)). There are no requirements for the CRAs to update their credit ratings as new information becomes available, and according to the SEC staff in practice the ratings are generally not updated.

Rule 38(3)(xi) requires the applicant for registration as a CRA to include in the application a sworn undertaking to keep such records as may be specified by the SEC from time to time.

A CRA has to have a minimum paid up capital of N20 million. The registration requirements under Rule 38 of the SEC Rules and Regulations include the requirement to submit information on the qualifications of at least two sponsored individuals (see Principle 29 for a definition of sponsored individual), but there are otherwise no specific requirements on the sufficiency of human resources.

**Oversight requirements: conflicts of interest**

Rule 38(4) of the SEC Rules and Regulations requires that the code of conduct for management and staff of a credit rating agency includes:

- a) a provision prohibiting key officers of the rating firm from investing in clients' shares;
- b) an undertaking to disclose to the SEC any shareholding interest of 5 percent and above of its directors and staff and their relatives in any issue to be rated;
- c) a provision specifying any relationship with clients;
- d) a provision for disclosure of its Board of Directors' interest in any of the rated issues;
- e) a sworn undertaking that undue advantage would not be taken of any unpublished price-sensitive information; and
- f) a provision on disciplinary measures for any misconduct or non-compliance by management and staff.

The employees of CRAs are also subject to the Code of Conduct for Employees of Capital Market Operators included in Schedule IX.2 of the SEC Rules and Regulations. Finally, the application for registration as a CRA has to include a sworn undertaking that every employee must display a high standard of professionalism and integrity in the conduct of his/her business.

|                      |   |
|----------------------|---|
|                      | <p>As for many other registered entities, the conflict of interest requirements apply only to the management and staff, but not to the CRA itself (see Principle 8). There are no requirements for the CRAs to disclose actual and potential conflicts of interest arising from the nature of compensation arrangements for producing credit ratings.</p> <p><b>Oversight requirements: transparency and timeliness</b></p> <p>There are no requirements for CRAs to distribute their credit ratings in a timely manner, to disclose credit ratings on a non-selective basis, to publish information about their procedures, methodologies and assumptions, or to publish information about the historical default rates of their credit ratings.</p> <p><b>Oversight requirements: confidential information</b></p> <p>The management and staff of CRAs are subject to the requirements to provide a sworn undertaking that they will not take undue advantage of unpublished price sensitive information (see above). There is no specific requirement for the CRAs to protect non-public information with respect to pending rating actions.</p>   |
| Assessment           | Partly Implemented  |
| Comments             | <p>The CRAs whose ratings are used for regulatory purposes in Nigeria are subject to a requirement to register with the SEC or, in the case of foreign CRAs, be exempted from registration. The SEC has sufficient powers to obtain information from the CRAs both through regular reporting and on an ad hoc basis, conduct inspections in the CRAs and take enforcement actions, including withdrawing and suspending a registration and imposing sanctions. So far the SEC has not conducted any on-site inspections in the CRAs, but has relied on reviewing their quarterly reports.</p> <p>The regulatory requirements address the four objectives of the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies (IOSCO Code) covered in Key Questions 4–7 of the IOSCO Methodology to a limited extent, and all CRAs do not seem to publish e.g., their rating methodologies or historical default rates on a voluntary basis.</p> <p>The SEC should expand its on-site inspection program to cover CRAs, and introduce sufficient conflict of interest requirements applicable also to the CRAs themselves, not only to their staff. It should also ensure the full implementation of the IOSCO Code, in particular given the anticipated increase in the demand for credit ratings in Nigeria.</p>            |
| <b>Principle 23.</b> | Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.  |
| Description          | <p><b>Regulatory framework for entities that provide analytical or evaluative services</b></p> <p>In Nigeria a market intermediary (e.g., a broker-dealer or portfolio manager) can provide analytical services ancillary to its main activities. An independent sell-side analyst would need an authorization as an investment adviser, but according to the SEC staff there are currently no such analysts in Nigeria.</p> <p>In addition, the Nigerian regulatory framework requires various providers of evaluative services to be registered as capital market consultants. They are the following professionals whose opinion impacts directly on capital market transactions (Rule 39 of the SEC Rules and Regulations):</p> <ul style="list-style-type: none"> <li>(i) Legal practitioners;</li> <li>(ii) Accountants;</li> <li>(iii) Auditors;</li> <li>(iv) Engineers;</li> <li>(v) Estate valuers; and</li> <li>(vi) Any other professional that may be determined by the SEC from time to time.</li> </ul> <p>The requirement for capital market consultants to be registered with the SEC was introduced because the SEC considered that such service providers should demonstrate sufficient knowledge of capital markets before being allowed to provide their services in these markets. A capital market</p> |

|   |  |
|---|--|
|   | <p>consultant is a type of Capital Market Operator (see Principle 29), and can be a body corporate, a partnership or an individual. They are subject to the same requirements as other Capital Market Operators.</p> <p><b>Sell-side securities analysts</b></p> <p><i>Conflicts of interest</i></p> <p>Since sell-side analysts are registered as Capital Market Operators, the Code of Conduct for Employees of Capital Market Operators (Schedule IX.2 of the SEC Rules and Regulations) applies to them. It imposes the following obligations on the employees of Capital Market Operators:</p> <ol style="list-style-type: none"> <li>1) Employees must disclose all transactions in securities made by themselves and their spouse, dependent children and relatives;</li> <li>2) Periodically, employees must submit to the management of the Capital Market Operator a statement of their personal securities investment portfolios;</li> <li>3) All new employees must at the time of assumption of duty lodge with their employer details of their holdings in long term securities of government and public companies;</li> <li>4) Although employees may be allowed to invest in securities of private companies, such investments must be disclosed to the employer when the affected company is about to go public.</li> </ol> <p>The above requirements apply only to the employees of sell-side analyst firms (as for other Capital Market Operators), and there are no conflict of interest rules applicable to the firms themselves. There are no regulations on the analysts' reporting lines and compensation arrangements.</p> <p><i>Compliance systems and senior management responsibility</i></p> <p>The Code of Conduct for Capital Market Operators (CMO) applicable also to sell-side analysts requires, among others, that the CMOs ensure that their employees maintain their securities trading accounts with their employers, where practicable, or provide full disclosure of such accounts and all trading activities to their employers. The CMOs are also required to monitor the transactions in securities by all their directors and employees and their spouses, dependent children and relatives.</p> <p>There is no requirement for written internal procedures or controls on the identification, elimination, management and disclosure of conflicts of interest. There are no particular requirements for procedures to eliminate or manage the undue influence of issuers, institutional investors and other outside parties upon analysts.</p> <p>The CMOs and their employees are subject to the requirement to not engage in any act that would adversely affect the general investing public's image of, and confidence in, the capital market. The CMOs are required to ensure that their employees act in a manner that is consistent with the best interest of their clients. Both the CMOs and their employees are subject to the requirement not to discriminate or give preferential treatment to any customer in the conduct of their professional business.</p> |
| Assessment  | Partly Implemented   |
| Comments  | <p>The Nigerian regulatory framework covers a particularly broad group of providers of analytical and evaluative services. Independent sell-side analysts would be regulated as investment advisers, but currently analytical services are provided only in connection with other investment services. To reach full compliance with this Principle, the SEC should ensure that its conflict of interest requirements are extended to cover all the elements of Key Question 3 of the IOSCO Methodology, in particular by including the firms themselves within the scope of the requirements and by introducing sufficient disclosure requirements.</p>   |
| <b>Principles for Collective Investment Schemes</b> |  |
| <b>Principle 24.</b>                                | The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a collective investment scheme.  |
| Description   | <p><b>Overview of the Nigerian regulatory framework for CIS and their operators</b></p> <p>The regulatory framework for collective investment schemes is set out in Part XIII of the ISA and</p>   |

Part H of the SEC Rules and Regulations. Section 153 of the ISA defines a collective investment scheme (CIS) as “a scheme in whatever form, including an open-ended investment company, in pursuance of which members of the public are invited or permitted to invest money or other assets in a portfolio, and in terms of which two or more investors contribute money or other assets to and hold a participatory interest and the investors share the risk and benefit of investment in proportion to their participatory interest in a portfolio of a scheme or on any other basis determined in the deed, but not a collective investment scheme authorized by any other Act.” According to the SEC staff, the reference to “CIS authorized by any other Act” relates to CIS registered in other jurisdictions.

The SEC may approve a collective investment scheme which is administered as a unit trust scheme, an open-ended investment company, or a real estate investment company or trust (Section 154 ISA) and may by notice published in the Gazette designate a scheme as constituting a collective investment scheme. According to Section 152 of the ISA, a unit trust scheme means any arrangement made for the purpose, or having the effect, of providing facilities for the participation of the public as beneficiaries under a trust in profits or income arising from acquisition, holding, management or disposal of securities or any other property. Unit trust schemes can be either open-ended or closed-ended. The latter are usually listed and traded on the NSE.

Currently most of the CIS in Nigeria are regular unit trusts (primarily open-ended) that invest in securities (see Section IV.). There are also two closed-ended, listed real estate investment trusts and seven closed-ended venture capital funds. The SEC has also recently facilitated the establishment of private equity funds through an exposed Rule 249D (see Principle 4 for comments on decisions made on the basis of exposed rules). Private equity funds can source funds only from qualified investors; currently only one such fund exists in Nigeria. There is also one ETF that is listed on the NSE, whose primary listing is on the Johannesburg Stock Exchange. The registration and listing of the ETF was facilitated through the issuance of SEC Rule 249B in January 2011, according to which an ETF can be a unit trust scheme, an open-ended investment company, or any other such structure approved by the SEC. The ETF listed on the NSE is in the form of a debenture.

Due to the predominance of unit trusts, the analysis in this Principle and Principles 25–27 focuses on them. The key parties to a unit trust scheme in Nigeria are the fund manager, trustee, custodian and registrar.

The functions of a fund manager are defined in Rule 188 of the SEC Rules and Regulations. The manager of an authorized scheme is not allowed to engage in any other activities than acting as a manager of a CIS and conducting other related activities.

Section 152 of the ISA defines a trustee as the person in whom the property for the time being subject to any trust created in pursuance of the scheme is or may be vested in accordance with the terms of the trust. A custodian means a person who has custody as a bailee of securities or certificates issued in the investor's name with the investor's name appearing in the issuer's register as the beneficial owner of the securities. In practical terms, a trustee has legal title to the assets of the funds, whereas the custodian holds the physical (or dematerialized) assets and manages the accounts of the fund.

According to Section 178 of the ISA, a manager must appoint either a trustee or a custodian for any scheme managed by it having regard to the structure of the scheme. However, since the enactment of Rule 239 in January 2011 the SEC has required that each fund has both a trustee and custodian. Trustees and custodians have to be registered with the SEC. The functions of a custodian are set out in Rule 239.

A registrar is defined in Section 315 of the ISA, and its functions are set out in Rule 193 of the SEC Rules and Regulations. The main task of the registrar is to keep the register of unit holders. The fund manager can itself act as the registrar, but in practice most fund managers use a separate registrar.

A trust deed is the agreement between the fund manager and the trustee. It governs the management of a unit trust scheme by laying down the rights, responsibilities, investment objectives, policies, outlets and all other relevant information for the fund.

## Registration and authorization requirements

### *CIS*

Section 160 of the ISA requires that collective investment schemes are authorized by and registered with the SEC. This is permitted where:

- the SEC is satisfied with the fitness and propriety of the manager and its directors, management, external auditors and trustee;
- the manager and trustee of the scheme:
  - (i) are bodies corporate incorporated under the CAMA;
  - (ii) have capital and reserves prescribed by the SEC from time to time; and
  - (iii) are registered by the SEC.
- the SEC is satisfied that the scheme is such that the effective control of its affairs is vested in the manager and exercised independently of the trustee of the scheme;
- the SEC is satisfied that the trust deed is in compliance with the ISA and the SEC Rules and Regulations; and
- the name of the scheme is not, in the opinion of the SEC, undesirable.

The SEC may refuse to authorize a scheme if it considers that the scheme fails to comply with the relevant provisions of the ISA. In such case, it has to notify the scheme's manager and trustee stating its reasons for refusal within sixty days of the filing of the application.

The requirements for the application for the authorization of a unit trust scheme and registration of its units are included in Rule 41(a)-(c) of the SEC Rules and Regulations. The SEC reviews all the documentation for each CIS before deciding to authorize a scheme and register its units (see Principle 26). The review is conducted by both a legal expert and a financial analyst.

### *Operating/marketing a CIS*

The manager of a CIS has to be incorporated under the CAMA and be a Capital Market Operator registered as a fund/portfolio manager (see Principle 29) with the SEC (Section 158 ISA). Contraventions of this provision are subject to a penalty of not less than ₦100,000 and a further sum of ₦5,000 per day during which the contravention continues.

The SEC may by regulation prescribe the qualifications and conditions for any person or institution to become or act as a manager or trustee (Section 179 ISA). A company or institution may not be a manager or trustee unless it maintains capital and reserves prescribed by the SEC. The SEC may not register a person as a trustee or custodian, if it is either a holding company, subsidiary or fellow subsidiary company of the fund manager (as defined in CAMA). The general financial and commercial standing and independence of a trustee and custodian also have to be such that they are fit for performing their functions. They also have to be sufficiently experienced and equipped to perform their functions.

The registration requirements for fund/portfolio managers are in Rule 37 of the SEC Rules and Regulations, whereas those applicable to trustees and custodians are included in Rules 35 and 27, respectively. The equivalent requirements for registrars are in Rule 34.

Section 155 of the ISA requires that a manager administers a collective investment scheme honestly and fairly; with skill, care and diligence; and in the interest of investors and the securities industry. Further, the manager of a scheme is required to (Section 157 ISA):

- avoid conflict between the interests of the manager and the interests of an investor;
- disclose the interests of its directors and management to the investor;
- maintain adequate financial resources to meet its commitments and to manage the risks to which its collective investment scheme is exposed;
- organise and control the scheme in a responsible manner;
- keep proper records;
- employ adequately trained staff and ensure that they are properly supervised; and
- have well-defined compliance procedures.

The specific functions of a unit trust manager are set out in Rule 41(d) of the SEC Rules and Regulations. Section 171 of the ISA requires the manager to invest the scheme funds in accordance with the trust deed with the objectives of safety and maintenance of fair returns on amounts invested.

Additional requirements on the code of conduct for Capital Market Operators and their employees that also apply to fund/portfolio managers, trustees and custodians are in Schedule IX of the SEC Rules and Regulations.

The requirement to be registered as a Capital Market Operator applies to a person that markets a collective investment scheme.

The practical registration process for fund managers is the same as for other Capital Market Operators (see Principle 29).

#### *Soliciting investment in foreign CIS*

According to Section 195 of the ISA, the SEC may approve an application by a manager or operator of a scheme administered in a foreign jurisdiction to solicit investment in such scheme from investors in Nigeria where the application complies with the conditions prescribed by the SEC and a copy of the approval or registration of the foreign collective investment scheme is filed with the SEC.

In the above cases, the SEC requires a local registered fund manager to be involved in the process, and the offering document has to comply with Nigerian requirements. In practice, the only foreign CIS currently marketed to Nigerian investors is the ETF listed on the NSE. Currently this ETF is also the only CIS registered in Nigeria whose custodian is located outside Nigeria.

### **Supervision and ongoing monitoring**

#### *Inspections and investigations*

In addition to the general power provided in Section 13(r) of the ISA for the SEC to call for information and inspect and conduct inquiries and audits of regulated entities and the power provided in Section 45 for it to conduct routine and special inspections and investigations of CMOs (see Principle 29 for a more detailed description), there are specific rules applicable to CIS and their managers. According to Section 172 of the ISA, the SEC may conduct an investigation into the business of any person, who is involved in the administration of a collective investment scheme or the soliciting of investment in a collective investment scheme.

The SEC's Collective Investment Schemes Department conducts yearly on-site inspections in registered fund managers and their trustees, registrars and custodians. The on-site inspection program is based on a quarterly plan. The inspections apply an extensive check list, and focus on compliance with the ISA and the SEC Rules and Regulations relating to CIS. They do not cover prudential aspects, such as capital level, internal controls or risk management, which would be covered in the inspections conducted by the Monitoring & Investigations Department. In case of shortcomings, the Collective Investment Schemes Department normally sends a letter to the regulated entity, requiring clarifications/explanations on the issues identified. The relevant inspection team is responsible for follow-up. In case of unsatisfactory reaction from the regulated entity, the case may be escalated to enforcement. In serious cases, the transfer to enforcement would happen in parallel to sending the letter. A quarterly summary inspection report is submitted to the Head of Department and, after feedback, to the relevant Executive Commissioner. The summary report reviewed appears thorough and includes many important observations. The Director-General is also informed through higher level summaries.

In addition to routine inspections, the Collective Investment Schemes Department conducts target inspections (on the basis of e.g., complaints or red flags). One such inspection was undertaken this year, and the case has since been transferred to enforcement. The SEC has also conducted some thematic inspections, e.g., in relation to the decision to prohibit the universal banking model in Nigeria to assess the impact on the schemes managed by bank subsidiaries.

As noted above, the inspections relating to fund managers' compliance with prudential requirements are the responsibility of the Investigations & Monitoring Department. Those inspections have been sporadic during the last three years, and have mainly been initiated on the basis of observations from quarterly returns (see Principle 12).

All SEC inspections are made unannounced, even though they would be based on an internal plan for regular inspections.

In 2010-2012 (to date), the Collective Investment Schemes Department has internally referred six cases to enforcement action due to e.g., commingling of fund's assets, misappropriation/borrowing

of fund's money and mismanagement of schemes (see Principle 12).

On the basis of Section 196 of the ISA, the SEC may appoint one or more competent inspectors to investigate and report on the managers, trustees and custodians of a CIS. Such an inspector is required to make a final report to the SEC on the conclusion of his investigation. The SEC may decide to provide a copy of the report to the persons concerned on request, and may also decide to publish the report. This possibility was used last time in 2009, when an external inspector joined a SEC inspection team.

#### *Periodic reporting*

The SEC is empowered to make regulations requiring periodic reports on the scheme to be prepared and submitted to the participants and the SEC (Section 186 ISA). According to Rule 41(1)(d)(vi) of the SEC Rules and Regulations, the unit trust managers have to file monthly and other periodic returns/reports with the SEC, the trustees of the fund, the registrars and unit holders. The requirement for the fund managers to send monthly and other periodic returns/reports relating to the scheme to the SEC is set out in Rule 205 of the SEC Rules and Regulations and its Schedules III and IV. On this basis, the SEC requires unit trust fund managers to submit monthly, quarterly and half-yearly returns, whereas venture capital/private equity fund managers and custodians to unit trust schemes submit only quarterly returns. The SEC does not currently enforce the above requirement for the manager to submit periodic reports to investors.

As an example, the monthly returns to the SEC require, among others, the unit trust fund managers to report for each fund the value of its investments per type of instrument (attaching valuation methods and analysis of valuation for all investments), number of unit holders, NAV, total number of units and information on progress in the preparation for the adoption of IFRS. The quarterly return covers some additional information, including on complaint handling. Finally, in the half-yearly return the unit trust fund managers have to, among others, provide a report on risk management, state any related party transactions, provide an update on the functioning of the investment committee, and provide information on the fund's accounting policies, performance and future outlook. Late returns attract a statutory penalty; in 2010–2012 (to date), 24 fines were given for late submission or non-submission of monthly or quarterly returns (see Principle 12).

Schedule IV. of the SEC Rules and Regulations requires the Capital Market Operators to file their annual report and accounts with the SEC. Late filing is subject to sanctions; 30 fines given in 2010–2012 (to date) totalled about ₦28 million (see Principle 12).

In addition to the above, the trustee of a CIS has the obligation to enquire into and prepare a report on the manager's administration of the scheme during each annual accounting period, stating whether the scheme has been administered in accordance with the ISA and the trust deed. If the manager has not complied with them, the trustee has to state the reason for the non-compliance and outline the steps taken by the manager to rectify the situation. There is a requirement for the report to be sent to the SEC and to the manager in good time to enable the manager to include a copy in its annual report. In practice, the SEC reviews the report from the annual report rather than requiring it to be submitted separately.

#### *Reporting of material changes*

A trustee must report to the manager any irregularity or undesirable practice concerning the collective investment scheme of which it is aware. If steps to rectify the irregularity or practice are not taken to the satisfaction of the trustee, it is required to report them as soon as possible to the SEC. Normally this happens by copying the SEC to the letter. Such letters have been sent rarely.

#### *Powers of the SEC*

In certain situations defined in Section 190 of the ISA, the SEC may give directives requiring the ceasing of the issue and/or redemption of the scheme units or winding up of the scheme, or appointing any person to take over the duties of the manager or trustee for an interim period. The SEC may also revoke or suspend the registration of a trustee, whenever it is no longer satisfied that the requirements contained in Section 179(3) of the ISA are met.

Section 187 of the ISA requires the manager of an authorized scheme to give written notice to the SEC of any proposed alteration to the scheme and any proposal to replace the trustee of the scheme. The trustee has to give written notice to the SEC of any proposal to replace the manager of the scheme, transfer the assets of the scheme to a new scheme or wind up the scheme. No effect can be given to any of these proposals unless the SEC has given its approval to the

|            |  |
|------------|--|
|            | <p>proposal, or one month has elapsed since the date on which the notice was given without the SEC having notified the manager or trustee that the proposal is not approved.</p> <p><b>Record-keeping</b></p> <p>As highlighted above, the CIS managers are subject to a general record-keeping requirement under Section 157 of the ISA. Further, Section 169 of the ISA requires that the manager of an authorized scheme causes proper books of account to be kept and annual accounts to be prepared which give a fair and true view of the affairs of the scheme. Finally, Section 186(2)(e) of the ISA authorizes the SEC to make regulations requiring the keeping of records with respect to the transactions and financial position of the scheme. However, such detailed regulations have not been made.</p> <p>Under Rule 41(1)(d) the managers of a unit trust fund have to maintain a schedule of unit holders, prepare periodic accounting records of the scheme and keep the books of the scheme. As noted above, the first task is in practice often undertaken by a registrar.</p> <p><b>Conflicts of interest and conduct of business</b></p> <p>As highlighted above, fund managers are subject to the requirement to avoid conflicts of interest (Section 157(1)(a)). There is no requirement to disclose conflicts of interest. Rule 247 of the SEC Rules and Regulations addresses certain conflicts of interest through trading prohibitions applicable to the management company, trustee and their affiliates.</p> <p>The CIS managers are subject to the Code of Conduct for Capital Market Operators and their Employees included in Schedule IX of the SEC Rules and Regulations. In this code, portfolio managers are subject to the specific obligation to exhibit diligence, thoroughness and competence in managing investors' funds. The clients' best interest must influence their investment decisions at all times. These requirements are also included in Section 155 of the ISA (see above).</p> <p>Sections 171(1) and 167(2)(d) of the ISA include general requirements for the manager to invest a scheme's funds with the objectives of safety and maintenance of fair returns and not to engage in any transaction that is not in the interest of unit holders and the scheme.</p> <p>There are no specific regulatory requirements on best execution, timely allocation, churning, related party transactions, underwriting arrangements and inducements.</p> <p>Rule 245 of the SEC Rules and Regulations requires that every unit trust prospectus contains a breakdown of the fees stating clearly that the management fee would be based on the net asset value of the fund. It also requires that the prospectus states that the initial expense is borne by unit holders and amortized over a maximum period of 5 years; this requirement is however in the process of being abolished. Rule 247 further requires that the annual management fee and the annual management fee plus other expenses cannot exceed 1.5 percent and 5 percent of the NAV of the fund, respectively, in addition to which the fund manager is entitled to an incentive fee not exceeding 30 percent of total returns in excess of 10 percent of the scheme's NAV per annum.</p> <p><b>Delegation</b></p> <p>There are no rules on delegation in the Nigerian legislative or regulatory framework. The SEC staff was of the view that in the Nigerian legal context this means that it is prohibited. In practice delegation is currently allowed to registrars maintaining the schedule of unit holders on behalf of the fund manager and to sub-custodians. In the case of sub-custody, the custodian remains liable under Section 155(2) of the ISA:</p> |
| Assessment | Broadly Implemented  |
| Comments   | <p>The Nigerian legislative and regulatory framework for fund management is fairly robust, and the SEC has introduced several new rules and regulations over the past few years. The purpose of these new rules has been both to expand the regulatory framework to facilitate the introduction of new products and to introduce certain additional safeguards to increase investor protection. The SEC's on-site inspection program relating to the schemes themselves is based on yearly inspections, whereas the fund manager itself is subject to less scrutiny (see Principle 29 for inspections conducted in the Capital Market Operators). Periodic reporting requirements are comprehensive.</p>   |

|  |  |
|--|--|
|  | The regulatory framework would benefit from further specifications to the requirements for the management of conflicts of interest (Key Question 12) and from the introduction of certain missing conduct of business rules (Key Question 14).   |
| <b>Principle 25.</b> The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets. |  |
| Description  | <p><b>Legal form</b></p> <p>The possible legal forms of a CIS are described under Principle 24. Before the manager of a scheme enters into a transaction with an investor, information that is necessary to enable the investor to make an informed decision must be given to the investor in a timely and comprehensible manner (Section 156 ISA).</p> <p><b>Investor rights</b></p> <p>The SEC is responsible for authorizing and registering a CIS. No manager, trustee or custodian is allowed to make any alteration to the trust deed or custodial agreement without the prior approval of the SEC (Section 162 ISA). Further, Section 187 requires the manager of an authorized scheme to give written notice to the SEC of any proposed alteration to the scheme (see Principle 24).</p> <p>The regulatory requirements for the contents of the trust deed for unit trusts are in Rule 247 of the SEC Rules and Regulations. The trust deeds generally provide for approval by investors before any change is made. The SEC pays attention to this while going through the documentation for a fund to be authorized and registered.</p> <p><b>Compliance with investment restrictions</b></p> <p>According to Section 171 of the ISA, a scheme fund has to be invested in accordance with the provisions of the trust deed with the objectives of safety and maintenance of fair returns on amounts invested. The ISA continues by noting that, subject to guidelines issued by the SEC from time to time, the funds and assets of a scheme must be invested in any of the following:</p> <ul style="list-style-type: none"> <li>(a) bonds, bills and other securities issued or guaranteed by the federal government and the CBN;</li> <li>(b) bonds, debentures, redeemable preference shares and other debt instruments issued by corporate entities listed on a securities exchange and registered under the ISA;</li> <li>(c) ordinary shares of public limited companies listed on a securities exchange and registered under the ISA with good track records having declared and paid dividends in the preceding five years;</li> <li>(d) bank deposits and bank securities of banks rated by rating agencies registered by the SEC;</li> <li>(e) investment certificates of closed-end investment funds or hybrid investment funds listed on a securities exchange and registered under the ISA with a good track record of earnings;</li> <li>(f) units sold by open-end investment funds or specialist open-end investment funds listed on the securities exchange recognized by the SEC;</li> <li>(g) real estate investment; and</li> <li>(h) such other instruments as the SEC may, from time to time, prescribe.</li> </ul> <p>A manager may also invest the funds and assets of a scheme in units of any investment fund provided that such investment fund may only be invested in the categories of investments set out above and in real estate. For the purpose of complying with any guideline set by the SEC as to the quality of instruments and banks that scheme assets may be invested in, and to ensure the safety of scheme assets in general, a manager is required to have due regard to the risk rating of instruments undertaken by a rating company registered by the SEC.</p> <p>The SEC has also allowed investments in unlisted equities in Rule 281A and up to 20 percent of the scheme's funds in Eurobonds of Nigerian entities on the basis of Section 171(2)(h) of the ISA. In case of non-compliance with the investment restrictions, the SEC proceeds in the same manner as in the case of findings from on-site inspections. The portfolio compositions are reported to the SEC in the monthly, quarterly and half-yearly reports.</p> <p><b>Segregation and safekeeping of assets</b></p> <p>Section 155(2) of the ISA requires that every authorized scheme adheres to the principle of segregation and identification. The SEC has issued rules on custodial services for CIS that require</p> |

|            |  |
|------------|--|
|            | <p>that a custodian be appointed by a scheme's fund manager with the approval of the SEC. The custodian has to, among others, be a registered financial institution with minimum shareholders' funds of ₦15 billion, have the professional and technical capacity to provide custodial services (where the custodian appoints a representative to act on its behalf such custodian will still be liable) and have adequately insured the assets in its custody against loss through fire, theft, natural catastrophe and the like, as well as taken out a fidelity guarantee cover, and have a system of internal controls which ensures that the assets under its custody are safeguarded and segregated and records adequately reflect the information they purport to present.</p> <p>The rules for CIS custodial services are in Rule 239 of the SEC Rules and Regulations issued in January 2011. They require that the custodian has to maintain adequate and proper books of accounts and records that include the following services:</p> <ul style="list-style-type: none"> <li>(a) Custody register: a collective investment scheme assets register in the name of each scheme/fund to which it acts as custodian;</li> <li>(b) Investment register: an investment register to record all investments effected and settled on behalf of the scheme;</li> <li>(c) Income collection register: a register of income received on a scheme/fund's investment, which must be categorized under income types (i.e., dividends, interest etc.).</li> </ul> <p>Further, Rule 239 requires that the custodian is subject to the requirement to have its assets separate and distinct from the scheme's assets and any other assets under its custody and be independent of a scheme's fund manager and trustee, and not be affiliated to either of the parties. In practice, the SEC has allowed the custodian and trustee to be affiliated parties, and it plans to amend Rule 239 to reflect the prevailing interpretation. Finally, except as may be authorized by the SEC, a person cannot act as a member of the board of directors or similar organ or as an officer responsible for the administration and management of the manager and at the same time hold a similar position with the custodian entrusted with the custody of the assets of any scheme managed by the manager.</p> <p><b>Winding up</b></p> <p>If the SEC, after an investigation or inspection under section 172, considers that the interests of the investors of a collective investment scheme or of members of the public so require, it may:</p> <ul style="list-style-type: none"> <li>(a) apply to the court under the CAMA for the winding-up of a manager of a collective investment scheme as if it were its creditor;</li> <li>(b) apply to the court for the appointment of a receiver in respect of a manager of a collective investment scheme as if it were its creditor;</li> <li>(c) require a manager to appoint, in accordance with the SEC's directions, in place of the serving trustee or custodian, a competent person nominated by the SEC;</li> <li>(d) require a manager to take steps, in accordance with the SEC's directions, for the winding-up of a portfolio of its collective investment scheme, and for the realization of its assets and the distribution of its net proceeds, together with any income accruals or other moneys available for distribution among the investors in proportion to their respective participatory interests;</li> <li>(e) direct a manager or a trustee or custodian to take any steps, or to refrain from performing or continuing to perform any act, in order to terminate or remedy any irregularity or undesirable practice or state of affairs disclosed by an investigation or inspection;</li> <li>(f) direct a manager to withdraw from the administration of a collective investment scheme, whereupon the trustee or custodian must in accordance with the SEC's directions arrange for another manager to take over the administration of the collective investment scheme; or</li> <li>(g) in the case of a collective investment scheme being administered in contravention of the ISA, apply to the court to have the collective investment scheme wound up, in which case the court may make any order it considers appropriate for the winding up of the collective investment scheme.</li> </ul> <p>The SEC may oppose any application for the winding up of a manager, a judicial management order in respect of a manager, or the winding up of a portfolio of a collective investment scheme. Any person who intends to make an application to that effect must give timely notice of such application to the SEC.</p> |
| Assessment | Fully Implemented  |

|   |   |
|---|---|
| Comments  | <p>The current requirements for the segregation and protection of client assets are comprehensive. The SEC has extensive powers to take various measures, including winding up of a CIS or a fund manager. Even though the current regulatory framework appears to be fairly robust, the rules have not been always been sufficiently enforced, and the open enforcement cases have the potential of undermining investor trust. The SEC, together with the relevant law enforcement authorities, should ensure that the cases are progressed with priority (see Principle 12 on further comments on the use of enforcement powers).</p>  |
| <p><b>Principle 26.</b> Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.</p> |   |
| Description   | <p><b>Initial disclosure obligations</b></p> <p>Section 156 of the ISA includes a general requirement for the manager of a scheme, before entering into a transaction with an investor, to disclose information about the investment objectives of the scheme, the calculation of the net asset value and dealing prices, charges, risk factors and distribution of income accruals, and give to the investor in a timely and comprehensible manner information that is necessary to enable the investor making an informed decision.</p> <p>According to Section 189(1) of the ISA, the manager of an authorized scheme is required to publish particulars of the scheme (scheme particulars) or make available to the public upon request any document containing information about the scheme in a manner prescribed by the SEC from time to time. The power of the SEC to approve the scheme particulars is based on Section 164 of the ISA, that requires that any letter, notice, circular or document prepared by the manager for the purpose of offering units or securities of a scheme to the public must be approved by the trustee and submitted to the SEC for approval before it is published. As highlighted in Principle 24, the SEC reviews all scheme particulars submitted to it for approval.</p> <p>The scheme particulars is referred to as prospectus in the SEC Rules and Regulations, which require the inclusion of, among others, the following information in the prospectus of a unit trust:</p> <ul style="list-style-type: none"> <li>(a) date of the prospectus;</li> <li>(b) name of the issuer/promoter, the fund manager and the registration number of the fund manager;</li> <li>(c) details on directors and principal officers of the manager;</li> <li>(d) names and addresses of the directors, managers and other parties to the issue;</li> <li>(e) type of units offered, amount offered, price and amount payable in full on application;</li> <li>(f) times of opening and closing of the offer;</li> <li>(g) management and advisory services;</li> <li>(h) names of the Investment Committee members specifying the independent members;</li> <li>(i) redemption policies;</li> <li>(j) name of the trustee and detailed information about it;</li> <li>(k) three to five years financial summary (the annual accounts have to be audited on the basis of Section 169 of the ISA<sup>6</sup>);</li> <li>(l) investment policy of the fund, including investment outlets;</li> <li>(m) duration of the scheme and conditions relating to its termination and modification of its trust deed; and</li> <li>(n) breakdown of the fees stating clearly that the management fee would be based on the net asset value of the Fund.</li> </ul> <p>The trust deed has to include, among others, the following information (Rule 247):</p> <ul style="list-style-type: none"> <li>(a) redemption of units by the managers at prices calculated in the manner prescribed under the SEC Rules and Regulations, and for their settlement to be effected not later than five working days following the transaction; and</li> <li>(b) investment policy, including investment outlets.</li> </ul> |

<sup>6</sup> Where the manager is a new company, it must furnish a statement of affairs including a financial projection

On the basis of the above, most of the information listed in Key Question 5 of the IOSCO Methodology is required to be included in either the prospectus or trust deed, with the exception of information on the methodology for asset valuation and information on custodial arrangements. In practice this information is however included in the prospectus. The prospectus is available from the fund manager or the SEC against a small fee.

#### **Ongoing disclosure obligations**

According to Section 189(2) of the ISA, regulations made by the SEC may:

- (a) require the manager of an authorized scheme to submit and publish or make available revised or further scheme particulars if:
  - i. there is a significant change affecting any matter contained in such particulars previously published; or
  - ii. a significant new matter has arisen.
- (b) provide for the payment of compensation to any person who has become or agreed to become participant in the scheme and suffered loss as a result of:
  - i. any untrue or misleading statement in the particulars; or
  - ii. the omission from the particulars of any matter required by the regulations to be included.

The SEC has not used its power to require issuers to submit and publish revised scheme particulars. However, in case of changes to the issues covered in the trust deed, the investors have to approve a supplemental trust deed.

#### **Information on valuation**

On the basis of Section 156 of the ISA, before the manager of a scheme enters into a transaction with an investor, the calculation of the net asset value and dealing prices must be disclosed to the investor. Rule 249 of the SEC Rules and Regulations requires that the calculation of prices at which units of any unit trust scheme may be bought or sold must be done in accordance with the formula in Schedule VI of the Rules and Regulations (see Principle 27).

#### **Periodic reporting**

Under Section 186(f) of the ISA, the SEC may make regulations requiring the preparation of periodic reports with respect to the scheme and the furnishing of those reports to the participants and the SEC. Under Rule 41(1)(d) of the SEC Rules and Regulations, the unit trust manager is required to prepare periodic accounting records of the scheme and file monthly and other periodic returns/reports with the SEC, the trustees of the fund, the registrars and unit holders. According to industry representatives, the Nigerian fund managers are generally aiming at providing their clients with half-yearly reports on the performance of the scheme.

The investors also have access to the report prepared by the trustee or custodian on the administration of the scheme from the annual report of the fund manager (see Principle 24).

The manager of an authorized scheme is required to cause proper books of account to be kept and annual accounts to be prepared which give a fair and true view of the affairs of the scheme. The accounts must be audited by a person appointed as auditor by the manager of the scheme with the consent of the trustee for the scheme. A copy of the auditors' report on the accounts and of such accounts certified by an auditor must be sent by the manager to the SEC and also published in national newspapers within three months after the end of the period to which the accounts relate.

The accounts for the financial year ending December 31, 2012, will need to be prepared on the basis of the IFRS (see Principle 18).

#### **Standard formats**

Rule 241 of the SEC Rules and Regulations requires that the information included in a prospectus of a unit trust scheme follows the order provided in Rules 245 and 247. Thereafter it does not need to follow any particular order, provided that the information is set forth in such a manner as not to obscure any required information necessary to keep it from being incomplete or misleading. The information set forth in the prospectus must be presented in a clear and concise manner under appropriate captions or headings reasonably indicative of the subject matter. The SEC is currently

|   |  |
|---|--|
|   | <p>considering how to revise the somewhat outdated standard contents requirements, and has therefore not actively enforced them.</p> <p>No standard format requirements apply to periodic disclosures.</p> <p><b>Advertisements</b></p> <p>Under Section 175 of the ISA, the SEC may object to the terms of any price list, advertisement, brochure or similar document relating to a scheme published or proposed to be published by a manager or any of its authorized agents, if the SEC considers the terms are calculated to mislead or are objectionable or undesirable. The SEC may direct the manager to discontinue or refrain from publishing or distributing any such document, or to amend its terms.</p> <p><b>SEC's powers</b></p> <p>Any manager under a scheme who buys or sells by means of a letter, notice, circular, document or oral communication which includes an untrue statement of a material fact, or omits to state a material fact necessary in order to make the statement, in the light of the circumstances under which it was made, not misleading, can become liable to the purchaser of such units or securities to recover the consideration paid for such units or securities, or for damages.</p> <p>The SEC's powers in relation to fund managers are discussed under Principle 29.</p>  |
| Assessment  | Broadly Implemented  |
| Comments  | The prospectus and trust deed provide fairly comprehensive information to investors to assist them in making their initial investment decision. The ongoing and periodic disclosure requirements are less developed, although in practice investors appear to have reasonably good access to such information through industry initiatives. The SEC should develop appropriate regulatory requirements in cooperation with the industry.   |
| <b>Principle 27.</b> Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme. |  |
| Description   | <p><b>Asset valuation</b></p> <p>Section 170 of the ISA requires that a unit or security is valued at its fair market price and authorizes the SEC to prescribe by regulation the mode and method of determining the fair market price.</p> <p>Schedule VI of the SEC Rules and Regulations provides that the bid and offer prices of units in a collective investment scheme are based on the net asset value (NAV) of the scheme calculated on a weekly basis by the scheme manager. The elements that are taken into account in the calculation of the NAV are:</p> <ul style="list-style-type: none"> <li>• total market value of securities based on the exchange daily official list as at the date of valuation (lowest market offer price).</li> <li>• stamp duties;</li> <li>• brokerage fee;</li> <li>• SEC fee;</li> <li>• actual cost of investment in unquoted companies;</li> <li>• estimate of capital appreciation for unquoted companies;</li> <li>• uninvested cash;</li> <li>• undistributed income to date less expenses; and</li> <li>• total value of money market instruments.</li> </ul> <p>Schedule VI. further provides that securities traded on a stock exchange or any regulated market will generally be valued at the last traded price quoted on the relevant exchange or market as at the date of computation. If no trade is reported for that date or if the exchange was not open on that day, the last published sale price or the recorded bid price (whichever is more recent) must be used. Prior to the adoption of Rule 281K of the SEC Rules and Regulations in January 2011, unlisted equity securities could be valued initially at cost and thereafter at the scheme's manager</p> |

|            |  |
|------------|--|
|            | <p>discretion. The new rule includes more guidance on the valuation of unlisted equities and emphasizes the role of the auditor. Unlisted securities (other than equities), for which there is an ascertainable market value will be valued generally at the last known price dealt on the market on which the securities are traded on or before the day preceding the relevant date of valuation and unlisted securities (other than equities), for which there is no ascertainable market value, will be valued at cost plus interest (if any) accrued from purchase to (but excluding) the valuation date plus or minus the premium or discount (if any) from par value written off over the life of the security. Any value otherwise than in Nigerian Naira must be converted at the prevailing market exchange rate.</p> <p>The auditor of a CIS is required to certify that the scheme has been operated according to the provisions of the ISA and the SEC Rules and Regulations, which covers valuation of the scheme's assets. When registering a CIS, the SEC is required to satisfy itself of the competence of, among others, the auditor of a CIS "in respect of matters of the kind with which they would be concerned in relation to a scheme." This appears to require that an auditor of a CIS would, among others, need to have specific expertise in assessing the valuation of the scheme.</p> <p>As highlighted under Principle 24, the monthly returns provided to the SEC require, among others, the unit trust fund managers to report for each fund the value of their investments per type of instrument (attaching valuation methods and analysis of valuation for all investments).</p> <p><b>Subscription and redemption</b></p> <p>Section 166(1) of the ISA provides that, whenever the holder of units or securities of an authorized scheme so requests, the manager under the scheme must buy from the holder the specified number of units or securities within the time prescribed by the SEC at the prevailing market price.</p> <p>Rule 247(d) of the SEC Rules and Regulations requires that the trust deed contains information on the redemption of units by the managers at prices calculated in the manner prescribed under the SEC Rules and Regulations, and for settlement to be effected not later than five working days following the transaction.</p> <p>There are no specific regulatory requirements for the disclosure of the price of the CIS to investors or provision of periodic statements to investors. The Fund Management Association of Nigeria has developed recommendations to its membership to provide at least weekly information to investors on the funds' prices either by email or on the fund managers' websites. Price information is otherwise available from newspapers, and for quoted unit trusts from the NSE.</p> <p><b>Pricing errors</b></p> <p>There are no specific regulatory requirements, rules or practices regarding pricing errors. According to the SEC staff, there have not been any cases of serious pricing errors in Nigeria.</p> <p><b>Suspension of redemptions</b></p> <p>Section 166(2) of the ISA provides that no manager of a scheme can suspend the right or postpone the date of redemption of units or securities by a holder except during public holidays or emergencies, when the stock exchange is closed or whenever the SEC permits it. Any manager of a scheme that contravenes the provisions of Section 166 of the ISA is liable to a fine of ₦500,000 and in addition to a penalty of ₦50,000 for every day the contravention continues.</p> <p>The SEC has not permitted the suspension of redemptions of the units of a CIS. However, in practice there are two funds whose redemptions have effectively been suspended since several years due to pending enforcement cases.</p> |
| Assessment | Broadly Implemented  |
| Comments   | The regulatory framework for the valuation of CIS assets and the pricing and redemption of the CIS units is fairly comprehensive. However, there are no specific regulatory requirements for the publication of unit prices or for the provision of periodic information to investors, or steps to be taken by fund managers in the case of pricing errors. In practice, these are currently dealt with through industry initiatives; it would however be recommendable that the SEC incorporates these into the regulatory framework in cooperation with the industry.  |

|   |   |
|---|---|
| <b>Principle 28.</b> Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight. |   |
| Description   |   |
| Assessment  | Not Applicable  |
| Comments  | There are currently no hedge funds in Nigeria and offering them would require changes to the SEC Rules and Regulations. Soliciting investment in a foreign hedge fund from Nigerian investors would need to be approved by the SEC; no applications have been made.   |
| <b>Principles for Market Intermediaries</b>   |   |
| <b>Principle 29.</b> Regulation should provide for minimum entry standards for market intermediaries.                                     |   |
| Description   | <p><b>Market intermediaries subject to registration</b></p> <p>According to Section 38(1) of the ISA, no person can operate in the Nigerian capital market as an expert or professional or in any other capacity as may be determined by the SEC, or carry on investments and securities business unless the person is registered in accordance with the ISA and the SEC Rules and Regulations.</p> <p>The Capital Market Operators listed in Rule 28 of the SEC Rules and Regulations subject to registration by the SEC that can be considered to fall under the IOSCO definition of market intermediaries are:</p> <ol style="list-style-type: none"> <li>1. issuing houses (distributors);</li> <li>2. underwriters;</li> <li>3. broker/dealers;</li> <li>4. sub-brokers;</li> <li>5. jobbers<sup>7</sup>;</li> <li>6. investment advisers; and</li> <li>7. fund/portfolio managers.</li> </ol> <p>The functions of broker/dealers (including sub-brokers), issuing houses, underwriters, fund/portfolio managers and investment advisers are defined in Rules 175, 183, 186, 188 and 193 of the SEC Rules and Regulations, respectively. Sub-brokers and investment advisers can be individuals, whereas only corporate bodies are qualified to be registered for the other above mentioned CMO functions.</p> <p><b>Registration requirements</b></p> <p>Section 38(2) of the ISA provides that the SEC must prescribe the conditions for registration including the level of knowledge and skill required to operate in the capital market.</p> <p>Rules 29–32 and 36–37 of the SEC Rules and Regulations provide the detailed registration requirements for the above mentioned intermediaries. As an example, an application for registration as broker/dealer has to be filed on Form SEC 3 contained in Schedule III to the SEC Rules and Regulations and accompanied by the following documents:</p> <ol style="list-style-type: none"> <li>(i) a minimum of two sets of completed Form SEC 2 to be filed by the sponsored individuals;</li> <li>(ii) a copy of Certificate of Incorporation certified by the Corporate Affairs Commission (CAC);</li> <li>(iii) a copy of Memorandum and Articles of Association certified by the CAC which, among others, must include the power to act as broker/dealer;</li> <li>(iv) a copy of Form C.O. 7 certified by the CAC;</li> <li>(v) a copy of the latest audited accounts or audited statement of affairs for companies in operation for less than one year;</li> <li>(vi) the profile of the company covering, among others, a brief history of the company, its organisational and shareholding structure, principal officers, etc. (see Form SEC 3 for details);</li> </ol> |

<sup>7</sup> According to the information provided by the SEC it does no longer register jobbers and there are currently no registered jobbers in Nigeria.

- (vii) a fidelity bond<sup>8</sup> representing 20 percent of paid-up capital;
- (viii) a sworn undertaking to keep proper records and render returns;
- (ix) a copy of the dealership certificate of the authorized dealing clerk being sponsored by the applicant;
- (x) evidence of minimum paid-up capital of ₦70 million; and
- (xi) any other information or document that may be required by the SEC from time to time.

The requirements for other market intermediaries are similar to the above.

*Fitness and propriety of directors and other responsible persons*

As part of their application for registration, those applicants that are corporate bodies have to also file information on their sponsored individuals on Form SEC 2 (either on two or three individuals depending on the function for which registration is sought). The information requested includes employment history, bankers (from which the SEC will request a reference), education, professional qualification, broker/dealer examination (if applicable), references (who will need to send a letter to the SEC), any disciplinary history, any criminal convictions and any bankruptcy or similar financial difficulties. Sponsored individuals are the principal officers and/or professionals held out by the applicant companies as experts, on whose advice or actions investors are expected to rely. In addition, the compliance officers of Capital Market Operators (see Principle 31) have to be registered as sponsored individuals with the SEC.

All sponsored individuals are required to undergo police clearance at the central criminal registry and provide satisfactory reports from their referees, bankers and previous employers. The police clearance requirement also applies to every partner, officer, director and chief executive. However, the latter group of individuals does not need to submit the SEC Form 2.

Companies registered/seeking registration to carry out multiple functions have to sponsor the total number of individuals prescribed for each function, except that in case of some related functions the applicant may sponsor only the minimum number prescribed for the lead function. This applies to issuing houses that also provide underwriting services and investment advice and broker/dealers that also provide fund/portfolio management services and investment advice.

*Fitness and propriety of shareholders*

The SEC collects basic information on the applicant's significant shareholders, but its fitness and propriety assessment does not extend to those shareholders or other persons that are in a position to exercise control or materially influence the applicant through a predetermined amount of ownership or voting power in the applicant. There are certain requirements on the fitness and propriety of shareholders in the CAMA, for the administration of which the CAC is responsible.

On the basis of Section 20 of the CAMA, an individual cannot join in the formation of a company if, among others, he is an uncharged bankrupt or disqualified under Section 254 of the CAMA from being a director of a company. A court is required to make an order that a person cannot be a director of or in any way concerned or take part in the management of a company for a specified period not exceeding 10 years, if:

- the person is convicted by a High Court of any offence in connection with the promotion, formation or management of a company; or
- in the course of winding up a company it appears that the person:
  - has been guilty of any offence for which he is liable (whether he has been convicted or not); or
  - has otherwise been guilty, while an officer of the company, of any fraud in relation to the company or of any breach of his duty to the company.

In addition, according to Section 80 of the CAMA, an individual cannot become a member (shareholder) of a company if he is of unsound mind and has been so found by a court in Nigeria or elsewhere, or he is an undischarged bankrupt.

<sup>8</sup> Every registered corporate body must provide and maintain a bond issued by an insurance company acceptable to the SEC against theft, fraud or dishonesty, covering each officer, employee and sponsored individual of the company.

***Initial capital requirements***

According to Rule 17, Rules 29–39 and Schedule I, Part B of the SEC Rules and Regulations the minimum paid-up capital for the various types of Capital Market Operators that are intermediaries under the IOSCO Principles is:

|                               |                   |
|-------------------------------|-------------------|
| Broker/dealer                 | 70 million        |
| Broker                        | 40 million        |
| Dealer                        | 30 million        |
| Corporate sub-broker          | 5 million         |
| Individual sub-broker         | net worth 500,000 |
| Underwriter                   | 100 million       |
| Issuing house                 | 150 million       |
| Fund/portfolio manager        | 20 million        |
| Corporate investment adviser  | 5 million         |
| Individual investment adviser | net worth 500,000 |

The minimum paid-up capital for multiple functions is the aggregate of the minimum paid-up capital of all the functions applied for (Rule 17(3) of the SEC Rules and Regulations).

***SRO membership***

Rule 42 of the SEC Rules and Regulations provides that, in addition to registering with the SEC, brokers and dealers are required to be members of one or more SROs. Where they effect transactions solely on a securities exchange of which they are a member, that exchange is the appropriate SRO. A broker or dealer needs to also be a member of an association of securities dealers to effect transactions in the OTC market (as referred to in Section 315 of the ISA). According to the SEC staff, this means that the members of the planned OTC trading platform to be operated by the NASD Ltd have to be members of the National Association of Securities Dealers.

**Registration process**

Except as otherwise directed by the SEC, all sponsored individuals of the applicants for registration have to appear before the SEC's Committee on Registration of Capital Market Operators and Institutions (Registration Committee) for interview to demonstrate that they possess sufficient knowledge of capital market operations. The meetings of the Registration Committee are held on prescheduled dates, e.g., in 2011 two prescheduled meetings took place. The meetings can be attended by a significant number of persons, e.g., in the June 2012 meeting 146 persons were present.

The SEC conducts a pre-registration inspection in all the companies applying for registration prior to the meeting of the Registration Committee. The inspections focus on ensuring that the applicant has appropriately equipped premises. In addition, its business plan, operational manual, organizational chart, and accounting and internal control procedures need to be enclosed to the application.

An internal memorandum is prepared after the pre-registration inspection that is submitted to the management for approval with the recommendation to invite the representatives of the applicant for registration interview with the Registration Committee. The memorandum provides information on whether the facilities of the applicant are adequate/in place. It also comments on the adequacy of the accounting and internal control systems and procedures of the applicant, but does not describe them. After the approval of the management, a standard format summary is prepared that is submitted to the Registration Committee for approval and further submission to the Board. This summary does not include any information on the observations made in the inspection beyond listing the documents reviewed and providing a recommendation on whether to register or not the applicant. On the basis of the documentation reviewed during the mission, the assessment of the companies applying for registration appears to focus on the assessment of its sponsored

individuals. While some internal procedures need to be enclosed in the application, they do not seem to play a primary role in the assessment.

According to Rule 29(3)-(4) of the SEC Rules and Regulations, the SEC must within 60 days after the filing of an application make known its decision to either grant or deny registration, unless the application is withdrawn. According to the information provided by the SEC, it received between January 2010 and July 2012 a total of 377 applications for registration of new companies as Capital Market Operators or for registration of additional sponsored individuals for previously registered Capital Market Operators. 336 persons attended the Registration Committee meetings. Out of these 336 attendants, 287 were approved and 49 were not approved. The data provided does not include information on how many companies' application for initial registration was rejected.

#### **Suspension or cancellation of registration**

According to Section 38(4)-(6) of the ISA, the SEC may by order suspend or cancel a certificate of registration. However, such an order cannot be made unless the person concerned has been given a reasonable opportunity of being heard (see Principle 2).

Rule 20B of the SEC Rules and Regulations further specifies that the SEC may suspend or cancel the registration granted to a Capital Market Operator or any registered function where the Capital Market Operator contravenes any of the provisions of the ISA, the SEC Rules and Regulations or the Code of Conduct for Capital Market Operators or fails to do any of the following:

- (a) furnish any information relating to its activities as required by the SEC or furnishes information which is false and misleading in any material particular;
- (b) submit periodic returns or reports as required by the SEC;
- (c) co-operate in any enquiry or inspection conducted by the SEC;
- (d) update its systems and procedures as recommended by the SEC;
- (e) resolve the complaints of clients or give a satisfactory reply to the SEC in this regard; or
- (f) meet renewal requirements.

The SEC may also cancel the registration granted to a CMO where it is found guilty of fraud or repeated defaults or convicted of an offence involving moral turpitude.

There are no requirements on a Capital Market Operator to cancel its registration once it has become inactive, even though Rule 20A of the SEC Rules and Regulations provides a process for that. Due to the fee structure of the SEC, neither do the operators have any incentive to cancel their registration (see Principle 2). There is apparently a significant amount of inactive CMOs in the market, but no data on the exact number of active Capital Market Operators exists.

According to the information provided by the SEC, it has last cancelled a registration of a CMO in 2008, when the registration of Thomas Kingsley Securities Ltd was cancelled. Consolidated information on the number of suspensions of registrations and the length of those suspensions was not available.

The SEC is also empowered to disqualify persons considered unfit from being employed in any arm of the securities industry (Section 13(bb) ISA). On the basis of Section 308 of the ISA, the SEC may also by notice require a Capital Market Operator to terminate the appointment of a director or officer of that Capital Market Operator, if he/she is no longer a fit and proper person to hold the office in question. When the SEC intends to act in this manner, it has to give notice of its intention and the reasons for that to the Capital Market Operator, and, unless it is impracticable to do so, to the director or officer concerned. In such cases, the director or officer has to cease to perform his/her functions pending the final outcome of an appeal (if any) to the IST. No information was available on the actual use of these powers.

#### **Ongoing requirements**

According to Section 307 of the ISA, a Capital Market Operator may not without the SEC's prior approval in writing change its registered name, shareholding or directors, use or refer to itself by a name other than its registered name or a literal translation thereof, or use or refer to itself by an abbreviation or a derivative of such name.

Rule 49 of the SEC Rules and Regulations requires all registered persons to file with the SEC

|   |   |
|---|---|
|   | <p>information on any major changes in the company that could affect the information filed in respect of the company's registration which at the time of registration was not known. This has to be filed in the appropriate form. Where these changes affect the audited accounts, the amended accounts have to be filed with the SEC within six months of the occurrence of the change.</p> <p><b>Publicly available information</b></p> <p>The SEC website includes information on the Capital Market Operators (both corporate bodies and individuals) and their permitted activities as of end of March 2011. The information is not up-to-date (see also above on inactive firms). The publicly available information does not cover the identity of the senior management and the names of other authorized individuals.</p> <p><b>Investment advisers</b></p> <p>The provision of investment advice, dealing, provision of custody services, and portfolio management are separate functions of a Capital Market Operator, each of which requires a registration for that particular function. Rule 192 of the SEC Rules and Regulations prohibits an investment adviser engaging in the maintenance or management of investors' funds. A Capital Market Operator registered only as an investment adviser cannot deal on behalf of a client, have custody of client assets, or manage client portfolios. Further, most of the requirements in the ISA and the SEC Rules and Regulations apply to all Capital Market Operators, including investment advisers.</p>  |
| Assessment  | Partly Implemented  |
| Comments  | <p>The SEC's registration process for new Capital Market Operators (companies) focuses on collecting information on the sponsored individuals. The process has two important shortcomings. Firstly, the fitness and propriety assessment is limited to 3–4 sponsored individuals, and does not necessarily cover all those in a position to materially influence the applicant (Key Question 2.(d) of the IOSCO Methodology). Similarly, the assessment of the shareholders of Capital Market Operators conducted by the CAC that the SEC relies on focuses on a very narrow set of issues. The SEC should complement that assessment with an assessment tailored to the needs of securities markets that would cover more information on any criminal or disciplinary history of the shareholders.</p> <p>Secondly, the preregistration inspection would benefit from a more extensive assessment of the sufficiency of the internal organization, risk management and supervisory systems of the applicant. It would be also be important that the management and the Registration Committee of the SEC would be provided with a description of those arrangements, rather than having to rely solely on the conclusion of the assessment made by staff.</p> <p>The ISA and/or the SEC Rules and Regulations should be revised to include a requirement for Capital Market Operators to withdraw their registration once they have become inactive. This could be complemented with a power provided to the SEC to automatically cancel the registration once a firm has been inactive for a certain period of time, without the need to resort to the enforcement measures provided in Section 20B of the SEC Rules and Regulations. The SEC should also seek to use its current powers to more actively suspend and cancel a registration of a Capital Market Operator in case of non-compliance.</p> |
| <p><b>Principle 30.</b> There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.</p> |   |
| Description   | <p><b>Capital and liquidity requirements</b></p> <p>The initial capital requirements of various types of Capital Market Operators are described in Principle 29. The net capital requirement included in Rule 48 of the SEC Rules and Regulations requires that all registered persons maintain the prescribed minimum paid-up capital. In addition, they are required to have at all times sufficient liquid assets to cover their current indebtedness. Broker/dealers are subject to the specific requirement not to permit their current indebtedness to exceed 200 percent of their net capital (Rule 176).</p> <p>Rule 17(4) of the SEC Rules and Regulations requires the cash/asset mix ratio for core operators in the market to be 60 percent liquid assets and 40 percent fixed and other assets while non-core operators' cash/asset mix ratio is required to be 30 percent cash and 70 percent fixed and other</p>   |

|            |   |
|------------|---|
|            | <p>assets. The concept of liquid assets is not defined in the Rule, but according to the SEC staff it has been interpreted to refer to cash and marketable securities. The concept of core operators was informed to refer to broker/dealers, portfolio managers, issuing houses and underwriters, whereas investment advisers are non-core operators. The SEC calculates this ratio on the basis of the balance sheet information provided to it in the quarterly/annual returns.</p> <p><b>Record-keeping, reporting and audit requirements</b></p> <p>On the basis of Section 39(1) of the ISA, a CMO is required to keep accounting and other records that sufficiently show and explain the transactions and financial position of its business and enable true and fair profit and loss accounts and balance sheets to be prepared regularly and in a manner that will enable them to be conveniently and properly audited. However, these record-keeping requirements do not address the need to be able to determine the capital levels at any time.</p> <p>Rule 170 of the SEC Rules and Regulations requires that every registered CMO (whether active or not) files with the SEC quarterly returns within thirty days after the end of the quarter and annual accounts certified by an auditor and prepared on a calendar or fiscal year basis not later than six months after the end of the accounting year.</p> <p>The quarterly return requires the following information on capital to be reported to the SEC:</p> <ul style="list-style-type: none"> <li>• SEC prescribed capital for function;</li> <li>• Paid-up share capital;</li> <li>• Reserves; and</li> <li>• Shareholders' funds</li> </ul> <p>In case of deficiencies in the capital levels, the SEC normally sends a letter to the Capital Market Operator. However, it is difficult for the SEC to take action in case of deficiencies unless it considers that the Capital Market Operator has failed or is failing or in crisis. On the basis of Section 13(v) of the ISA, the SEC has in such cases the power to intervene in the management and control of a Capital Market Operator, including entering into its premises and doing whatever else the SEC deems necessary for the protection of investors. In addition, the SEC can use the powers available to it under Sections 48-50 of the ISA (for a detailed description of these powers, see Principle 32).</p> <p>In its on-site inspections and through the quarterly reports, the SEC has identified many Capital Market Operators that have been in the need of immediate recapitalization. Due to the lack of audit trail in the various supervisory steps that the SEC has taken in relation to particular cases, it has not been possible to verify how those cases were ultimately resolved. Neither has the SEC been able to provide data on how many CMOs' registration has been suspended or cancelled due to insufficient capital.</p> <p>The NSE also monitors the capital adequacy of its dealing members through quarterly reporting and on-site inspections and has suspended members due to inadequate shareholders' funds (see Principle 34).</p> <p><b>Unlicensed affiliates</b></p> <p>The Nigerian prudential framework for market intermediaries does not address risks arising from outside the regulated entity, for example from unlicensed affiliates.</p> |
| Assessment | Not Implemented   |
| Comments   | <p>The initial capital requirements of Capital Market Operators are very low compared to the nature and amount of business expected to be undertaken by various types of CMOs. The current capital requirements are not structured to result in capital addressed to the full range of risks (e.g., credit, market and operational risks) to which market intermediaries are subject, nor are they sensitive to the quantum of risks undertaken or designed to allow an intermediary to absorb some losses and to wind down its business over a relatively short period (Key Questions 2–4 of the IOSCO Methodology).</p> <p>The record-keeping and reporting requirements are not sufficient to determine and monitor the development of the capital level of an intermediary (Key Questions 5 and 6). The SEC has limited powers to intervene in case a CMO's capital level deteriorates; neither has the SEC been effective in using its existing intervention powers (Key Question 9). The Nigerian prudential framework does</p>   |

|                      |   |
|----------------------|---|
|                      | <p>not currently address risks from outside the intermediary (Key Question 10).</p> <p>The SEC is currently planning to move to a risk-based supervisory framework, one element of which would be a change in the capital requirements. Sufficient details were not available at the time of the assessment mission to evaluate to which extent the planned changes would improve the compliance of the Nigerian capital requirements with the IOSCO Principles. The introduction of any new capital requirements should be combined with increasing the ability of the SEC to intervene earlier than currently in the case of deteriorating capital levels. The SEC should also improve its internal ability to take immediate action in case of a need.</p> <p>Finally, the Nigerian authorities are planning to introduce consolidated supervision of financial institutions. At the time of the mission, it was unclear to which types of groups consolidated supervision would apply, and what their impact on groups including Capital Market Operators would therefore be.</p>   |
| <b>Principle 31.</b> | <p>Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.</p>  |
| Description          | <p><b>Role of management</b></p> <p>The registration requirements for CMOs require information to be provided on the profile of the company, including a brief history of its organizational structure, shareholding structure and principal officers. There are no other requirements on the management and organizational structure of CMOs.</p> <p>There are no specific requirements for the management to bear primary responsibility for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the whole firm. Neither does the regulatory framework include any specific requirements about management information systems or procedures to maintain the security, reliability and integrity of the information provided to the management.</p> <p><b>Internal control and risk management</b></p> <p>The Nigerian regulatory framework does not include any specific requirements on internal controls and risk management of CMOs. The CMOs are not required to be subject to an objective, periodic evaluation of their internal controls and risk management processes. There are no requirements on the segregation of key duties and functions.</p> <p>There is a specific requirement in Rule 99 of the SEC Rules and Regulations to make all payments for purchase or sale of securities either by personal cheque or bank draft, except for amounts not exceeding ₦50,000.00. In addition to this very specific requirement relating to the integrity of CMOs' dealing practices, the Capital Market Operators are subject to the requirements arising from the anti-money laundering legislation, including those covered in the SEC's Anti-Money Laundering/Combating Financing of Terrorism Compliance Manual for Capital Market Operators.</p> <p><b>Compliance function</b></p> <p>Rule 168B of the SEC Rules and Regulations requires that every Capital Market Operator appoints a compliance officer who is responsible for monitoring compliance with the ISA and the rules and regulations, notifications, guidelines, instructions etc. issued by the SEC or the federal government. The CMO has to register the compliance officer with the SEC as a sponsored individual. The compliance officer is required to immediately and independently report to the SEC any non-compliance observed by him. The SEC staff interviewed was not aware of any reports from compliance officers that would have been sent to the SEC.</p> <p><b>Conflicts of interest</b></p> <p>There is no general requirement in the Nigerian regulatory framework requiring a CMO to endeavor to address a conflict of interest between its interests and those of its clients or between its clients. There is no requirement for the intermediaries to have mechanisms in place to manage conflicts of interest where the potential for them arises.</p> <p>The Code of Conduct for Employees of Capital Market Operators (Schedule IX.2 of the SEC Rules and Regulations) imposes certain obligations on the employees of CMOs. They are required to ensure that their personal interest does not at any time conflict with their duty to their employer's</p> |

clients. They must also ensure that their advice on investment decisions is not beclouded by any conflict of interest. The client's best interest must be given priority over the employees' personal interest. The employees are not entitled to engage in any activity which might directly or indirectly influence their judgment prior to or during a business transaction.

Rule 103(1) of the SEC Rules and Regulations requires that a securities dealer must not, whether as a principal or on behalf of a person associated with him, buy or sell securities if its client has instructed it to buy or sell securities of the same class and it has not yet complied with the instruction. This rule does not prevent the dealer from entering into a transaction as a principal or on behalf of a person associated with him, if the instruction from the client requires the purchase or sale of securities to be effected only subject to specified conditions and the dealer has been unable to complete the transaction due to those conditions.

#### **Direct electronic access**

Direct electronic access is not facilitated in the current trading system of the NSE.

#### **Client assets**

Section 40 of the ISA requires that a CMO maintain separate accounts for transactions carried out on behalf of different clients. No CMO can mix the proceeds of the account of a client with those of other accounts whether belonging to the Capital Market Operator or its clients. More specifically, Section 40(3) of the ISA requires that a Capital Market Operator establishes and keeps in a bank or banks one or more trust accounts to be designated or evidenced as trust accounts, into which it must pay:

- a) all amounts (less any brokerage and other proper charges) received from or on account of any person (other than a Capital Market Operator) for the purchase of securities which are not attributable to securities delivered to Capital Market Operator; and
- b) all amounts (less any brokerage and other proper charges) received for or on account of any person (other than a Capital Market Operator) from the sale of securities which are not paid to that person or as that person directs not later than the next banking business day following the day on which they were received by the Capital Market Operator.

Rule 178 of the SEC Rules and Regulations requires that a broker/dealer keeps at all times separate accounts for every client transaction and prohibits the broker/dealer to engage in the following acts:

- a) mixing of client's funds with the funds of the broker/dealer in a single account;
- b) mixing of securities carried for the account of a customer with securities carried for the accounts of any other customer or self;
- c) pledging of any securities of a client to borrow in the ordinary course of business as a broker/dealer;
- d) use of client's funds to purchase securities not specified in the prior mandate of the client;
- e) alteration of the client's mandate without obtaining the prior consent of the client;
- f) use of client's uninvested funds for purposes other than for the benefit of the client; and
- g) any other act that may be specified by the SEC from time to time for the protection of investors.

According to the SEC staff, the requirement for separate accounts for the clients' funds can be complied with by keeping records of clients' funds at the level of the CMO, i.e., there is no requirement to open an individual bank account for each client. However, the CMO's and clients' funds can never be held in the same account. The current securities settlement system operated by the CSCS requires the establishment of a separate securities account for each client.

The Nigerian regulatory framework for client asset protection does not include any specific measures facilitating the transfer of positions and assisting in the orderly winding up of the Capital Market Operator in the event of its financial insolvency and the related need to return the client assets.

#### **Investor complaints**

The Nigerian regulatory framework does not include a specific requirement for CMOs to provide for a mechanism to address investor complaints. However, the broker/dealers, portfolio managers and investment advisers are required to include in their quarterly returns to the SEC information on complaints received and resolved and those passed to the SEC or the NSE.

**Know your customer requirements**

Rule 100 of the SEC Rules and Regulations requires CMOs to obtain information about their clients before entering into a binding contract. For this purpose, they need to demand, among others, the following:

- (a) Individuals:
- (i) Names;
  - (ii) Mother's maiden name;
  - (iii) Residential address;
  - (iv) Next of kin;
  - (v) Passport photograph;
  - (vi) Thumb print (where applicable);
  - (vii) Signature;
  - (viii) Any form of identification, including driver's license, international passport or national identity card;
  - (ix) Employer's name and address or vocation and place of business;
  - (x) Purpose and reason for opening the account or establishing the relationship;
  - (xi) Sources of wealth or income and expected origin of the funds to be used during the relationship;
  - (xii) Place of domicile; and
  - (xiii) Home town/state of origin.
- (b) Institutional (corporate) investors:
- (i) Name and address;
  - (ii) Certificate of incorporation certified by the CAC;
  - (iii) Memorandum and articles of association certified by the CAC;
  - (iv) CAC form showing list and particulars of directors certified by the CAC;
  - (v) CAC form on return of allotment of shares, showing share structure, certified by the CAC;
  - (vi) Purpose and reason for opening the account or establishing the relationship; and
  - (vii) Expected origin of the funds to be used during the relationship.

Where a customer is acting on behalf of another person, e.g., someone else is supplying the funds, or the investment is held in the name of someone else, the Capital Market Operator is required to verify the identity of the client as well as the third party to ensure that the audit trail for the funds is preserved. Capital Market Operators must require duly executed power of attorney from a party purporting to act on behalf of another in the sale or purchase of securities. A power of attorney executed abroad has to be registered in Nigeria before it can be relied upon by a CMO.

Where a customer fails to provide satisfactory identification within a reasonable time, a CMO is not allowed to open the account, commence a business relationship or perform the transaction. Where money has been deposited, the CMO has to make a suspicious transaction report to the EFCC and the SEC.

Where a potential customer, customer or beneficial owner is a politically exposed person<sup>9</sup>, the decision to open the account or to continue the relationship has to be taken at senior management level, and the Capital Market Operator has to ascertain the source of funds.

As noted above, the CMOs have to obtain from their prospective clients information on the clients' employer's name and address, vocation and place of business; the purpose and reason for opening the account or establishing the relationship; and the sources of wealth or income and expected origin of the funds to be used during the relationship. The requirements do not directly cover the obligation to obtain and retain information on the investment objectives relevant for the services to be provided. However, the above elements aim at gaining information also on the customer's investment objectives.

<sup>9</sup> A politically exposed person includes a serving or former political appointee in any tier of government of the federation or their agencies and their relations such as wives, brothers, sisters, children and other close relations.

**Record-keeping requirements**

In addition to the requirements of Section 39 of the ISA, Rule 47 of the SEC Rules and Regulations specifies that all registered persons must keep and maintain all books, records and financial reports required under the ISA and the SEC Rules and Regulations. They have to be maintained and preserved in a readily accessible place for a period of not less than five years from the end of the year during which the last entry was made on such record, the first two years in an appropriate office of the registered person.

Rule 177 of the SEC Rules and Regulations requires that a broker/dealer maintains proper and adequate records of transactions for and on behalf of each client. Such records must include among others:

1. mandate forms;
2. contract notes;
3. clients' statements of accounts;
4. deposit receipts for purchase of shares;
5. scrip receipts to certify deposits;
6. exact prices at which the shares were bought or sold; and
7. full details of the fees charged on secondary market transactions.

Further, there are specific record-keeping requirements for portfolio managers in Rule 189 of the SEC Rules and Regulations.

**Information to clients**

There are no requirements in the Nigerian regulatory framework requiring market intermediaries to provide the clients a written contract of engagement, an account agreement or a written form of the general and specific conditions of doing business through the market intermediary. Neither are there any particular regulatory requirements to disclose or make available information to the clients so that they can make an informed investment decision.

With regards to information required on transactions executed on behalf of clients, Section 98 of the ISA requires that a securities dealer must, within the prescribed time and in respect of every securities transaction made either as a principal or agent, issue a contract note. The contract note has to include the following information (Section 99 ISA):

- (a) the name and style under which the securities dealer carries on his business and the address of the principal place at which the business is carried on;
- (b) the name and address of the person to whom the securities dealer gives the contract note;
- (c) the date on which the transaction took place and, if outside a securities exchange or capital trade point, a statement to that effect;
- (d) the number, amount and description of the securities which are the subject of the contract;
- (e) the price per unit of the securities;
- (f) the amount of the consideration;
- (g) the rate and amount of commission (if any) charged;
- (h) the amounts of all stamp duties or other duties and taxes payable in connection with the contract; and
- (i) if the settlement amount with or without benefit is to be added to or deducted from the settlement amount in respect of right to a benefit purchased or sold together with the securities, the first-mentioned amount and the nature of the benefit.

Section 44 of the ISA also requires that a Capital Market Operator or a custodian supplies on demand to its client copies of all entries in its books relating to any transaction carried out on behalf of that client. It is entitled to levy a reasonable charge for providing the copies. A client or any person authorized by the client is entitled at any time, free of charge, to inspect any contract notes and vouchers relating to the transaction.

Rule 179 of the SEC Rules and Regulations requires that every broker/dealer furnishes its clients with:

- (i) a quarterly report of the client's accounts showing all purchase transactions on behalf of the client including the statement of account for the period; and
- (ii) a quarterly report detailing the client's share portfolio, including the statement of share ownership from the clearing and settlement agency.

In addition, every broker/dealer is required to provide a client on demand a statement of account

|            |  |
|------------|--|
|            | <p>showing both credit and cash transactions made on behalf of the client.</p> <p>If a fund manager has custody or possession of clients' funds or securities, it has to send each client monthly an itemized statement showing the funds and securities in the custody or possession of the fund manager as at the end of the period and all debits and credits in the client's accounts during the period (Rule 191(1)(e)).</p> <p><b>Best interest of clients</b></p> <p>The Code of Conduct for Capital Market Operators (Schedule IX.1(iv) of the SEC Rules and Regulations) requires that all CMOs ensure that their employees act in a manner that is consistent with the best interest of their clients. To this end, Capital Market Operators must preserve the confidentiality of all clients' information.</p> <p><b>Supervisory program</b></p> <p>Section 13(r) of the ISA empowers the SEC to call for information and inspect and conduct inquiries and audits of regulated entities. Further, Section 45 of the ISA requires the SEC to conduct routine and special inspections and investigations of CMOs.</p> <p>The on-site inspections of broker-dealers and the on-site prudential inspections of other Capital Market Operators are conducted by the Monitoring &amp; Investigations (M&amp;I) Department. In addition to these inspections, the Collective Investment Schemes Department has its own on-site inspection program that focuses on inspecting compliance with the legal and regulatory requirements for CIS and their managers, trustees and custodians. The Securities &amp; Investments Departments also conducts pre- and post-transaction inspections in issuing houses that focus on inspecting compliance with the initial disclosure requirements. The various inspections are not coordinated.</p> <p>In 2010, the M&amp;I Department conducted only 13 on-site inspections at CMOs, and no on-site inspections were made in 2011. In 2009, 23 CMOs were subject to on-site inspections. The 2009-2011 inspections were for cause inspections, i.e., at the time of the assessment mission the SEC had not conducted any routine on-site inspections in Capital Market Operators for at least the past three and a half years.<sup>10</sup> In those inspections, the CMOs' capital level, status of operations, asset quality, liquidity, indebtedness, validity of fidelity bond, know-your-customer rules and audited accounts are normally inspected. A summary of the 2011 inspections was reviewed during the assessment mission. There were significant findings that had led to internal recommendations for supervisory and enforcement actions. Due to the reasons highlighted in Principle 30, it has not been possible to verify what action the SEC has taken on the basis of those on-site inspections.</p> <p>The SEC's limited on-site inspection program is complemented by the on-site inspections made by the NSE. It has not been possible to assess the comprehensiveness and quality of the NSE's on-site inspection program during the mission beyond noting the total number of inspections made and the topics covered in those inspections (see Principle 34).</p> |
| Assessment | Partly Implemented   |
| Comments   | <p>The most important conduct of business rules are in place in Nigeria, but the legislative and regulatory framework would require enhancements to organizational requirements, emphasizing the responsibility of the management (Key Questions 1 and 2 of the IOSCO Methodology), internal controls (Key Questions 1, 3 and 5), risk management (Key Questions 3 and 5) and management of conflicts of interest (Key Question 6). Strengthening the legal basis for these requirements would provide important backing to the SEC's planned move to risk-based supervision.</p> <p>The SEC should prepare its on-site inspection program in a coordinated manner across the departments. The current product-driven inspections should be complemented or, where appropriate due to the planned transition to risk-based supervision, replaced with inspections that focus more on ensuring that the CMOs have sufficient internal control, risk management and compliance processes in place.</p>   |

<sup>10</sup> After the assessment mission, the SEC has conducted some on-site inspections in Capital Market Operators selected on the basis of observations from the quarterly reports.

|                      |   |
|----------------------|---|
|                      |   |
| <b>Principle 32.</b> | There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.   |
| Description          | <p><b>Early warning systems</b></p> <p>The only mechanism in place for the SEC to give it notice of a CMO's potential default is the quarterly reporting that includes information on, among others, capital. Early warning signs can also be received through the complaints received by the SEC.</p> <p><b>Plans</b></p> <p>The SEC does not have any specific plans for dealing with the eventuality of a firm's failure.</p> <p><b>Powers</b></p> <p>As highlighted under Principle 30, the SEC has the power to intervene in the management and control of a Capital Market Operator which it considers has failed or is failing or in crisis, including entering into the premises and doing whatever it deems necessary for the protection of investors (Section 13(v) ISA).</p> <p>Section 48 of the ISA provides that where the SEC is satisfied that the Capital Market Operator is in a grave situation, or the CMO informs the SEC that it is likely to become unable to meet its obligations under the ISA, about to suspend its obligations to any extent, or insolvent, the SEC may by order in writing exercise any one or more of the following powers:</p> <ul style="list-style-type: none"> <li>(a) prohibit the Capital Market Operator from receiving funds or other assets from the public for a certain period (extendable);</li> <li>(b) require the Capital Market Operator to take any steps or refrain from doing something within a stipulated time period;</li> <li>(c) remove any manager or officer of the Capital Market Operator;</li> <li>(d) notwithstanding any limitations in the law or in the constitutive documents of a company as to the minimum or maximum number of directors: <ul style="list-style-type: none"> <li>(i) remove from office any director of the Capital Market Operator; or</li> <li>(ii) appoint any person or persons to manage the affairs of the Capital Market Operator in the interim;</li> </ul> </li> <li>(e) appoint any person to advise the Capital Market Operator in relation to the proper conduct of its business.</li> </ul> <p>If, despite steps taken under Section 48 of the ISA, the state of affairs of the Capital Market Operator concerned does not improve significantly, the SEC may assume control of the whole of the property and affairs of the Capital Market Operator, carry on the whole of its business and affairs, assume control of such part of the CMO's property, business and affairs as it considers necessary, or appoint persons to do so on its behalf (Section 49 ISA).</p> <p>If the SEC or an appointed person has assumed control of the business of a Capital Market Operator, the Capital Market Operator is required to submit its capital market business to the control of the SEC and to provide the SEC or the appointed person with such facilities as they may require to conduct the business.</p> <p>Where the SEC or an appointed person has assumed control of the business of a Capital Market Operator, it must remain in control of and continue to carry on the business of the Capital Market Operator in the name and on behalf of the Capital Market Operator until such time as:</p> <ul style="list-style-type: none"> <li>(a) the SEC is satisfied that adequate provision has been made for the repayment of investors; or</li> <li>(b) in the opinion of the SEC, it is no longer necessary for the SEC to remain in control of the business of the Capital Market Operator.</li> </ul> <p>The cost and expenses of the SEC or the remuneration of an appointed person is payable from the funds and properties of the Capital Market Operator as a first charge on its funds.</p> <p>Where the SEC or an appointed person has, pursuant to an order under section 49 of the ISA, assumed control of a Capital Market Operator whose paid-up capital is lost or unrepresented by available assets, the SEC may make an order revoking the Capital Market Operator's registration and apply to the Federal High Court for an order for the SEC or any person nominated by it to purchase or acquire the Capital Market Operator for a nominal fee for the purpose of its</p> |

|            |   |
|------------|---|
|            | <p>restructuring and subsequent sale.</p> <p>Before any of the above orders is made, the Capital Market Operator, and where relevant, the director, manager or officer who is to be removed from office, have to be given a reasonable opportunity of making representations against the proposed order. The SEC, after due consideration of any such representation, may either confirm, modify, alter, vary or replace the earlier order.</p> <p>Where the SEC makes an order revoking the registration of a Capital Market Operator and requiring its business to be wound up, the Capital Market Operator is required, within fourteen days of the date of the order, to apply to the Federal High Court for an order winding up the CMO's affairs. The Federal High Court must hear the application in priority to all other matters. If the Capital Market Operator fails to apply to the Federal High Court within the above period, the SEC may apply to the Federal High Court for the winding up of the Capital Market Operator.</p> <p>If satisfied that it is in the public interest to do so, the SEC may, without waiting for the 14 day period to elapse, appoint any person as the official receiver or provisional liquidator. The person so appointed has the power conferred under the CAMA.</p> <p><b>Investor compensation schemes</b></p> <p>Section 197 of the ISA requires a securities exchange or capital trade point to establish and maintain an investor protection fund. An investor protection fund must be administered by a board of trustees subject to the supervision of the SEC. The assets of an investor protection fund have to be vested in the board of trustees and kept separate and applied for the purposes as set out in the ISA.</p> <p>The objectives of an investor protection fund are to compensate investors who suffer pecuniary loss arising from (Section 198 ISA):</p> <ul style="list-style-type: none"> <li>a) the insolvency, bankruptcy or negligence of a dealing member firm of a securities exchange; or</li> <li>b) defalcation committed by a dealing member firm or any of its directors, officers, employees or representatives in relation to securities, money or any property entrusted to, or received or deemed received by the dealing member firm in the course of its business as a Capital Market Operator.</li> </ul> <p>Further requirements relating to the governance and constitution of the investor protection fund and payments to be made out of its funds are in Sections 199-221 of the ISA. The Nigerian Stock Exchange has established an investor protection fund, but it is not yet operational.</p> <p>Section 13(k) of the ISA also requires the SEC to establish a nationwide trust scheme to compensate investors whose losses are not covered under the investor protection funds administered by securities exchanges and capital trade points. According to the information provided by the SEC staff, the SEC is in the process of setting up such a trust scheme, but the details were not available at the time of the mission.</p> <p><b>Communication and cooperation with other regulators</b></p> <p>The SEC is a member of the Financial Services Regulatory Coordinating Committee composed of Nigerian regulatory authorities (see Principle 1). This provides a channel for communication and cooperation between domestic regulators, even if its processes and procedures do not directly address cooperation in relation to financial disruption of individual firms.</p> <p>The SEC has entered into MoUs with foreign securities regulators (see Principle 14), that can provide a basis for cooperation in case of financial disruption in e.g., a foreign-owned Capital Market Operator.</p> |
| Assessment | Partly Implemented  |
| Comments   | <p>The SEC should, preferably in cooperation with the other members of the FSRCC, formalize a written plan for dealing with a failure of a Capital Market Operator, based on different possible failure scenarios and their impact on the Nigerian financial system.</p> <p>None of the two investor protection funds required to be established under the ISA by the SEC and the NSE, respectively, is yet in operation. The SEC should seek to find an expeditious solution to</p>  |

|   |  |
|---|--|
|   | the current situation.   |
| <b>Principles for the Secondary Markets</b> |  |
| <b>Principle 33.</b>                        | The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.   |
| Description                                 | <p><b>Authorization of exchanges and capital trade points</b></p> <p>One of the functions of the SEC is to register and regulate securities exchanges, capital trade points, futures, options, derivatives and commodity exchanges, and any other recognized investment exchanges in Nigeria (Section 13(b) ISA).</p> <p>A securities exchange is defined in Section 315 of the ISA as an exchange or approved trading facility such as a commodity exchange, metal exchange, petroleum exchange, options, futures and other derivatives exchange, and an over-the-counter (OTC) market. An exchange is defined as being any exchange registered by the SEC pursuant to the ISA which constitutes, maintains or provides a market place for bringing together purchasers and sellers of securities or for otherwise performing the functions commonly performed by an exchange with respect to securities.</p> <p>In Nigeria, no securities of a public company listed on any recognized securities exchange can be bought or sold outside the facilities of a recognized exchange on which the securities are listed (Section 106(4) ISA). Therefore OTC equity trading is currently limited to unlisted equities. According to the SEC staff, the OTC trading in its current bilateral format does not require registration, but setting up an organized "OTC trading" platform would be subject to registration by the SEC as an OTC market.</p> <p>A capital trade point is defined as a mini exchange registered by the SEC pursuant to the ISA, which constitutes, maintains or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing, with respect to securities, the functions commonly performed by a securities exchange (Section 315 ISA).</p> <p>Section 28 of the ISA provides that no securities exchange or capital trade point can commence operation unless it is registered with the SEC. Due to the above wide definition of a securities exchange, it appears that the requirement to register as a securities exchange applies not only to exchanges organizing trading in securities (shares and fixed income securities), but also to derivatives and commodity exchanges and OTC markets. An application for registration as an exchange, OTC market or capital trade point has to be made to the SEC in the form and manner specified by the SEC.</p> <p>The only securities exchange currently operating in Nigeria is the Nigerian Stock Exchange (NSE). In addition, the Abuja Securities &amp; Commodity Exchange (ASCE) is registered as a commodity exchange, but it is currently not organizing any trading. There are no futures, options, or other derivatives exchanges in Nigeria, neither have any capital trade points been registered yet. NASD Ltd has been granted an Approval-in-Principle for registration of an OTC market subject to certain conditions, including satisfactory pre-registration inspection and satisfactory performance of NASD Ltd and its sponsored individuals at the registration meeting.</p> <p>The NSE is currently owned by its members, but the SEC established in September 2011 a Technical Committee to examine the processes for demutualizing the NSE. The Committee delivered its report on March 2, 2012, and the SEC is currently considering on how to proceed with the issue.</p> <p><b>Authorization criteria</b></p> <p>Every securities exchange and capital trade point has to be a body corporate incorporated under the CAMA (Section 29 ISA). The SEC may register a body corporate as a securities exchange or capital trade point if it is satisfied that the rules of the body corporate make satisfactory provisions:</p> <ol style="list-style-type: none"> <li>for the exclusion from its membership persons who are not of good character and who do not possess a high degree of business integrity;</li> <li>for the expulsion, suspension or discipline of members for conduct inconsistent with just and equitable principles in the transaction of securities business or for contravention of or failure to</li> </ol> |

- comply with the rules of the securities exchange or capital trade point or the ISA;
- c) with respect to the conditions under which securities may be listed for trading on that particular securities exchange or capital trade point;
  - d) with respect to the conditions governing dealings in securities by the members;
  - e) with respect to the class or classes of securities which may be dealt by members; and
  - f) with respect to a fair representation of persons in the selection of the Board members of the securities exchange or capital trade point and the administration of its affairs, provided that listed companies and investors are each represented by one or more members on its board.

The SEC is required to ensure that the interest of the public will be served by the registration of a securities exchange or capital trade point.

More detailed registration requirements for securities exchanges are included in Rule 22 of the SEC Rules and Regulations. They include a requirement to accompany the application with the following documents:

- existing or proposed by-laws or rules and rules of the exchange (including a code of conduct and code of dealing);
- listing requirements;
- sworn undertaking to promptly furnish the SEC with copies of any amendments to the rules of the exchange and the listing requirements;
- information relating to market facilities including
  - trading floors/facilities;
  - quotation board;
  - information board/ticker tape,
- detailed information about the trading system to be adopted;
- information as to the exchange's organization including structure and profile of the members of its Council/Board as well as rules and procedures;
- instruction and inspection manual of members' activities;
- detailed information about the promoters and principal officers of the exchange;
- an application for registration of at least three principal officers of the exchange;
- minimum paid-up capital requirement of ₦500 million; and
- any other document required by the SEC from time to time for the protection of investors.

The SEC may not register an exchange nor allow its registration to remain in force if its rules do not provide for expulsion, suspension or discipline of members for conduct or procedure inconsistent with just and equitable principles of trade. The SEC has to inform the applicant about its decision to either grant or deny registration within 60 days after the filing of the application, unless the application is withdrawn by the applicant.

Similar requirements as for exchanges are set out for capital trade points in Rule 24 with the only notable difference relating to the capital requirement for the latter being only ₦20 million instead of ₦500 million.

The NSE does not assume principal, settlement, guarantee or performance risk.

#### **Ongoing conditions**

Section 31 of the ISA requires that where an amendment is made to the rules or listing requirements of a securities exchange or capital trade point, their boards need to forward a written notice of the amendment to the SEC for approval. The SEC notifies them as to whether it approves the whole or any specified part of the amendment in question, and until such notification is received, the amendment is of no effect.

The responsibilities of a securities exchange and capital trade point in market surveillance and member supervision are described in Principle 34, together with the requirements for the related disciplinary procedures.

There are no particular requirements for the exchanges'/capital trade points' technical system standards and procedures related to operational failure. Assessment of the mechanisms that are in place to identify and address disorderly trading conditions and to deal with any contravening

conduct (e.g., through trading halts, where appropriate) is not required by the regulatory framework. However, two members of the SEC staff are present in the NSE premises on a continuous basis during trading hours, and are therefore in a position to address and escalate any issues arising.

Securities exchanges and capital trade points are subject to the requirement to maintain proper books of account and records relating to their operations, which have to be made available for inspection by the SEC (Section 37 ISA).

Securities clearing and settlement companies also need to be registered by the SEC, and they have to enclose their rules and regulations to their application (Rule 25 of the SEC Rules and Regulations). Therefore the SEC has access to the information on how trades are cleared and settled.

The Nigerian regulatory framework does not specifically address outsourcing. According to the SEC staff, non-core activities of securities exchanges and capital trade points (such as distribution of market data) can be outsourced, and such outsourcings have taken place.

### **Securities and market participants**

#### *Securities*

As noted above, the listing requirements of securities exchanges and capital trade points are subject to the approval of the SEC (Section 31 ISA). Further, all securities of a public company have to be registered with the SEC, as required in Sections 13(d) and 54 of the ISA.

The only product types currently admitted to trading on the NSE are equities and bonds. Unit trusts are admitted to memorandum listing, i.e., they are not traded. In addition, one ETF is admitted to trading on the NSE.

#### *Market participants*

In addition to the issues related to the admission criteria of the NSE highlighted in Principle 9, the regulatory framework does not include any requirements on fair access to the securities exchange for those that have been admitted as members.

### **Order execution procedures**

There are no particular requirements in the Nigerian regulatory framework on disclosure of order routing procedures and execution rules to market participants. The rules of the exchange have to be submitted to the SEC for approval, but the current order execution rules of the NSE are limited to the provisions of Article 76 on maintenance of trading systems and Article 100 on pricing methodology. The former requires that the NSE provide an automated trading system to be referred to as The Nigerian Stock Exchange Automated Trading System (The NSEATS). The latter makes reference to the fact that the opening and closing prices are generated by the trading engine on any given day, that price movement can only occur as a result of a transaction whose volume is not less than that prescribed by the NSE, and that the price movement band on any given trading day must be as determined by the NSE. Disclosure on the functioning of the trading engine happens through training of dealing clerks and presentations given to exchange members.

The rules of the NSE require that each dealing member must maintain the appropriate systems and technology to enter customers' orders and receive reports and trading data electronically from the NSE's trading systems. A dealing member must also maintain the required electronic linked facilities with the CSCS and maintain an off-site back-up system for data to prevent any problems in its electronic systems.

The SEC does not review the trade matching algorithm of the NSE. There are no regulatory requirements on equality of technical access or disclosure of differences in order execution response times. There are no regulatory requirements on systems and controls, including automated pre-trade controls that enable intermediaries to implement appropriate risk limits. However, according to the NSE, sponsored access to its trading system is currently not possible.

|                      |  |
|----------------------|--|
|                      | <p><b>Access to information</b></p> <p>The NSE Rules and Regulations are available on its website. As noted above, their content is however very limited when it comes execution rules.</p> <p>Even though securities exchanges are subject to the general record-keeping requirement under Section 37 of the ISA, there is no specific regulatory requirement on maintaining a sufficient audit trail to reconstruct trading activity within a reasonable time.</p> <p>There are no particular regulatory requirements on the pre- and post-trade information that needs to be provided to members of a securities exchange to enable them to implement appropriate monitoring and risk management controls in relation to direct electronic access/sponsored access. However, as noted above, this type of access to the NSE's trading system is currently not possible.</p>   |
| Assessment           | Partly Implemented   |
| Comments             | <p>Various types of organized trading platforms are subject to registration in Nigeria. The regulatory framework is unclear in terms of differences between a securities exchange, capital trade point and OTC market. As the definition of a securities exchange covers OTC markets, according to the ISA the latter would need to be subject to the same requirements as a securities exchange. The definition of a capital trade point refers to it being a "mini exchange", but does not include any additional indications of what would constitute "mini".</p> <p>At the moment when new platforms start emerging in Nigeria, it is important that additional clarity will be provided on the distinction between various types of trading platforms and their regulatory treatment. There seems to be a need to revise the relevant provisions of the ISA and/or the SEC Rules and Regulations to ensure that each type of platform will be appropriately regulated rather than applying different criteria only through interpretations of the SEC.</p> <p>In the current circumstances, where the NSE is the only registered trading platform in Nigeria, there are few regulatory requirements on the trading system in relation to many of the elements covered by Principle 33. This applies in particular to issues covered in Key Questions 5 and 6 of the IOSCO Methodology. Given the planned adoption of a new, more sophisticated trading system at the NSE and the possible introduction of an OTC market, it is important that sufficient regulatory requirements are introduced and that, in parallel, the SEC increases its supervisory expertise and the scope of its supervisory activities in this area.</p> <p>The SEC will need to ensure that the rules of the NSE to be adopted when the new trading system will be introduced will provide significantly more transparency than the current rules on the order execution procedures also to other market participants than dealing members. The SEC also needs to pay attention to the rules and arrangements regarding equality of access to the exchange, both in terms of membership criteria and technical access.</p> |
| <b>Principle 34.</b> | There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.   |
| Description          | <p><b>Market surveillance</b></p> <p><i>SEC</i></p> <p>The SEC has two of its staff members present at the NSE premises during trading hours to monitor trading. As part of this surveillance, the staff monitors announcements made by listed companies, and reports to the management any suspicious activities around those announcements. The SEC also has the possibility to monitor unusual transactions due to the requirement on registered broker/dealers to disclose to the SEC any single deal in a company's securities of 500,000 units and above within a day. It has electronic access to the trading system from the Lagos zonal office, but currently not from Abuja.</p>   |

During the past one year, the SEC has initiated investigations on insider trading in a few cases. Those cases are still pending.

#### **NSE**

The NSE conducts market surveillance in its market surveillance department that employs three persons. It follows trading and news throughout the day, and can be alerted to unusual developments in the market through the alerts from the trading system when specific trigger points have been reached. The NSE is planning to acquire a more sophisticated market surveillance system.

#### **Member supervision by the NSE**

As a securities exchange, the NSE is required to call for information from, inspect and conduct inquiries and audits of its members (Section 32(2) ISA). The NSE's right to examine the activities of Capital Market Operators is included in Rule 169 of the SEC Rules and Regulations, which require the Capital Market Operators to permit a duly authorized officer of an SRO to examine their activities and records.

The NSE has to file at the end of every quarter a detailed report on its surveillance and enforcement activities with the SEC. The report includes financial information on the number and names of firms inspected (as part of regular plan and in spot checks) and certain key data on each firm (capital adequacy and certain liquidity, profit, debt management, and efficiency ratios). Secondly, the report includes a summary (in yes/no format) on the compliance by the inspected dealing members with certain requirements (record keeping, quality of management, infrastructure, and certain internal control and contingency measures). In addition to the quarterly report, the NSE also has the obligation to furnish copies of all examination reports of its members to the SEC within 30 days after the end of the quarter in which the inspection was carried out (Rule 169). These reports are submitted to the Registration and Recognized Investment Exchanges Department rather than the Monitoring & Investigations Department that is responsible for the ongoing supervision and on-site inspections of broker-dealers.

The NSE also requires the dealing members to file their quarterly financial statements with it.

If the NSE reprimands, fines, suspends, expels or otherwise takes disciplinary action against its members, it is required to notify within seven days the SEC in writing of the name and other particulars of the member and the nature of and reason for the action taken against the affected member (Section 33 ISA). In 2011 and 2012, the NSE suspended the trading rights of its dealing members almost 600 times. Most of the suspensions were undertaken due to reporting delays.

| <b>Reason for suspension</b>   | <b>2011</b> | <b>2012<br/>(January-June)</b> |
|--|-------------|--------------------------------|
| Failures relating to quarterly reports (non-submission, discrepancies, incorrect format) | 36          | 255                            |
| Failures relating to annual accounts (non-submission, late submission)                   | 72          | 62                             |
| Failure to resolve various complaints  | -           | 10                             |
| Inadequate shareholders' funds   | 64          | 5                              |
| Failure to appoint substantive MD/CEO  | 3           | 2                              |
| Failure to comply with NSE directives  | 22          | 2                              |
| SEC action   | 7           | 2                              |
| Failure to adhere to deadlines on fines issued by the NSE                                | -           | 1                              |
| Non-compliance with inspection report  | 43          | -                              |
| <b>Total</b>   | <b>247</b>  | <b>339</b>                     |

No other disciplinary measures than suspensions have been taken by the NSE in 2011 and 2012.

The SEC's supervision and enforcement of broker/dealers are described under Principles 12 and 31.

|            |   |
|------------|---|
|            | <p><b>SEC's supervisory and enforcement activities in relation to the NSE</b></p> <p>The supervision of the NSE during the past three years has been undertaken in extraordinary circumstances, where the SEC has used not only its supervisory but also its enforcement powers under the ISA. With regards to inspections, the SEC has the power to call for information from and inspect and conduct inquiries and audits of securities exchanges and capital trade points (Section 13(r) ISA). As for enforcement powers, the SEC has at its disposal the same tools as for other regulated entities (see Principle 10). Further, on the basis of Section 35 of the ISA the SEC may, where it deems appropriate, issue directives to a securities exchange with respect to:</p> <ul style="list-style-type: none"> <li>a) trading on or through the facilities of the securities exchange or pertaining to any securities listed;</li> <li>b) the manner in which a securities exchange carries on its business including the manner of reporting off-market purchases; or</li> <li>c) any other matter which the SEC considers necessary for the effective administration of the ISA.</li> </ul> <p>The SEC conducted an on-site inspection at the NSE in 2009. After the inspection, the SEC set up bi-monthly meetings with the NSE at the Executive Management level, and more frequent technical level meetings. However, according to the SEC the management of the NSE was reluctant to attend these meetings. This together with the findings of the 2009 inspection, complaints from key stakeholders, financial condition of the NSE, and its corporate governance deficiencies led to the SEC intervening by using its enforcement powers under Sections 13, 35, 47, 48, 49 and 308 of the ISA. In August 2010, the SEC issued a directive to the then CEO of the NSE to remove her from office for failure to comply with the SEC's earlier directives and to satisfy the SEC that the NSE continues to be subject to the effective supervisory oversight of the Council.</p> <p>Following this intervention, the SEC appointed an interim administrator who updated the SEC Board at every Board meeting. The interim administrator was charged with recruiting the new management team of the exchange, and the SEC participated in this process as an observer. He was also tasked with undertaking the initial arrangements to upgrade the trading platform, address the corporate governance lapses identified and develop the legal framework for demutualization. To assist the interim administrator and to further strengthen governance at the exchange, the SEC in April 2011 nominated eight public interest members to the Council of the Exchange.</p> <p>Due to the above measures, the SEC has not considered it necessary to conduct an on-site inspection at the NSE in 2010 and 2011. It has a planned a routine inspection for 2012, which would also evaluate progress in the terms of reference for the public interest members of the Council.</p> <p>As noted in Principle 33, the rules of a securities exchange and capital trade point need to be approved by the SEC. There are no specific regulatory requirements on a securities exchange to monitor its risks.</p> <p><i>Withdrawal of authorization</i></p> <p>On the basis of Section 30 of the ISA, the SEC may by order revoke the certificate of registration granted to a securities exchange or capital trade point if it ceases to operate, is wound up, or is operating in a manner detrimental to the interests of investors and the public.</p> <p>Rule 20B of the SEC Rules and Regulations regarding the suspension and cancellation of the registration of a Capital Market Operator applies also to a securities exchange (see Principle 29).</p> |
| Assessment | Broadly Implemented   |
| Comments   | Since 2009, the supervision of the NSE has been undertaken in extraordinary circumstances that culminated to the enforcement measures undertaken in August 2010. This has lead to a situation where an on-site inspection has not been considered necessary. The quarterly reporting from the exchange has continued in the normal manner. It is important that the SEC resumes its normal  |

|   |   |
|---|---|
|   | <p>supervisory role vis-à-vis the exchange as soon as possible.</p> <p>As highlighted in Principle 9, it would be important that the SEC and NSE agree on their division of responsibilities in market surveillance and member supervision. Depending on the agreed divisions of responsibilities, it is important that the market surveillance capacity of the SEC and/or the NSE will be enhanced through the use of a more sophisticated market surveillance system than currently. The SEC should also ensure that the NSE widens the use of the disciplinary measures available to it beyond suspensions in more serious cases.</p>  |
| <b>Principle 35.</b> Regulation should promote transparency of trading.   |   |
| Description   | <p>The Nigerian regulatory framework does not include any requirements for providing pre- and post-trade information to market participants. The SEC does not have any role in determining the appropriate pre- and post-trade transparency standards in the Nigerian securities markets, since they are not addressed in the execution rules of the NSE and the SEC does not review the trade matching/order execution algorithm or information system of the NSE. The extent of pre- and post-trade transparency information to be provided to the market is therefore left to the discretion of the NSE and other possible future trading systems.</p> <p>According to oral information given by the NSE, the only derogation from pre-trade transparency currently applies to iceberg orders. The functionality of iceberg orders is built within the trading system. With regards to post-trade transparency, it was informed that price and volume data is provided real-time to subscribers and that there is no possibility to delay publication of post-trade transparency information e.g., in the case of large trades. During the assessment mission, it was not possible to have access to the trading and market information system to confirm the nature of the pre- and post-trade transparency information currently provided. The SEC staff was not aware of the arrangements in place, and in discussions with some market participants it was indicated that the information might not in practice be complete and available on a real-time basis.</p>  |
| Assessment  | Not Implemented   |
| Comments  | <p>On the basis of the oral information provided by the NSE, the current pre- and post-trade transparency information provided by the NSE would appear to be in line with the IOSCO Principles. However, the regulatory framework or the NSE rules do not specify those requirements or broader objectives for market transparency. The conditions for derogation(s) from pre-trade transparency and waivers from post-trade transparency are not clearly defined as required by Key Question 2(a) of the IOSCO Methodology.</p> <p>The SEC staff was not able to confirm the nature and extent of the pre- and post-trade information available and the arrangements in place for its distribution and publication. Further, the discussions with market participants indicated that there might be deficiencies in the completeness and availability of pre- and post-trade transparency information.</p> <p>Defining clear and equitable requirements on pre- and post-trade transparency has been a key focus of securities regulators in the past few years. Partially this has been caused by increased level of competition between various trading platforms and the related need to avoid the creation of increasingly non-transparent trading platforms for competitive reasons. In the current Nigerian circumstances with one monopoly provider for equity trading services, similar concerns do not yet exist. However, the lack of involvement of the SEC in setting the appropriate transparency requirements is not in line with the IOSCO Principles and good regulatory practices. In addition, the current pre- and post-trade transparency arrangements of the NSE should be clearly defined and disclosed also through other means than the trading system that is accessible only to dealing members.</p> |
| <b>Principle 36.</b> Regulation should be designed to detect and deter manipulation and other unfair trading practices. |   |
| Description   | <p><b>Prohibition of market abuse</b></p> <p>Sections 103 and 105–111 of the ISA and Rules 110 and 133 of the SEC Rules and Regulations</p>   |

|  |   |
|--|---|
|  | <p>prohibit various types of market abuse:</p> <ul style="list-style-type: none"> <li>• front running;</li> <li>• market manipulation;</li> <li>• disclosure of false or misleading statements;</li> <li>• use of fraudulent means; and</li> <li>• insider dealing.</li> </ul> <p>Directors and other insiders of a company are subject to a requirement to notify their sales and purchases in the company's shares no later than 48 hours after the transaction (Section 111 ISA).</p> <p>Under Section 115 of the ISA, the criminal liability for contravening the above prohibitions would be a fine of at least ₦500,000 (for individuals) or an amount equivalent to double the amount of profit derived or loss averted by the use of the information obtained in contravention of any of the above provisions, or imprisonment for a term not exceeding seven years. For bodies corporate the minimum fine would be ₦1,000,000.<sup>11</sup></p> <p>In addition, Section 116 of the ISA provides that a person found to be liable must pay compensation to any person who suffered a loss as a result of the contravention. The amount of compensation would be the amount of the loss sustained by the person claiming the compensation or any other amount as may be determined by the SEC or the IST.</p> <p><b>Regulatory approach</b></p> <p>The market surveillance activities of the SEC and NSE are described in Principle 34. At least during the past three and a half years (2009 to date), the market abuse cases that the SEC has taken to the IST or forwarded to the criminal authorities have been limited to those identified in connection with the work of the Joint Task Force with the CBN (see Principle 12). The SEC and NSE have not imposed administrative sanctions on market abuse.</p> <p>The SEC and NSE were not able to provide information on whether the NSE has referred any market abuse cases to the SEC for further investigation during the past few years.</p> <p><b>Trading suspensions</b></p> <p>On the basis of Section 36 of the ISA, where the SEC deems it necessary for the protection of persons buying or selling particular securities of a body corporate on a securities exchange, it may suspend or prohibit further trading in the securities and give notice in writing to the securities exchange. If, after receiving the notice, the securities exchange fails to take action to prevent trading in the securities, the SEC may prohibit trading in the securities of the body corporate during a period not exceeding 14 days. The SEC has the power to increase the period for a further period not exceeding 30 days at a time.</p> <p>A securities exchange which permits trading in securities in contravention of the SEC's order is liable to a penalty of ₦1,000,000 and a further sum of N50,000 for every day during which the contravention continues.</p> <p>Where, after the expiration of the second period of suspension of trading in the securities of a body corporate, the body corporate or securities exchange still refuses to comply with the SEC's directives, the SEC may:</p> <ol style="list-style-type: none"> <li>a) revoke the registration of either or both the body corporate and the securities exchange;</li> <li>b) refuse to consider or process any further request or application for approval, registration or consent made or to be made to the SEC by the body corporate or securities exchange;</li> </ol> |
|--|---|

<sup>11</sup> Contravening the front running prohibition is however subject to a fine of N100,000-500,000.

|  |   |
|--|---|
|  | <p>c) apply to the Court under the CAMA for:</p> <ul style="list-style-type: none"> <li>(i) the winding up of the body corporate or securities exchange;</li> <li>(ii) an official receiver to take over, under court supervision, the management of the registered company or securities exchange, as if the SEC were its creditor.</li> </ul> <p>d) after giving a hearing to serving officers, appoint competent person(s) in place of the serving chief executive officer, executive management and board of the registered company or securities exchange;</p> <p>e) apply to the IST for an enforcement order in respect of its directive to suspend trading in the specified securities.</p> <p>The SEC may take any of the above actions where it considers that the interest of investors or of members of the public or the integrity of the market so requires.</p> <p><b>Cross-market trading</b></p> <p>Since the NSE is the only securities exchange in Nigeria and there are no derivatives exchanges, there is no domestic cross-market trading. There are also no foreign linkages or direct foreign participation at the NSE.</p>   |
| Assessment   | Partly Implemented  |
| Comments   | <p>The regulatory framework prohibiting market abuse is in place in Nigeria. However, the SEC's and NSE's surveillance and enforcement activities have led to limited results, even though certain improvements have recently been achieved through joint efforts by the SEC and CBN. No administrative measures have been taken. The current mechanisms for combating market abuse in Nigeria do not therefore appear to be effective. On the basis of the information available, it is not possible to assess whether this is due to surveillance or enforcement deficiencies.</p>  |
| <b>Principle 37.</b> Regulation should aim to ensure the proper management of large exposures, default risk and market disruption. |   |
| Description  | <p><b>Monitoring of large exposures</b></p> <p>The securities settlement system operated by the CSCS that is connected to the NSE verifies that a seller has the securities in its account in the CSCS before they can be sold. Article 33 of the NSE Rules requires that, unless otherwise stipulated at the time of a transaction, all shares dealt in by a dealing member are deemed to be fully paid. Further, it requires any offer to buy or sell at a price named to be funded. This means that a dealing member should verify that the client has the funds to pay for the securities bought. If the client fails to pay, the responsibility lies with the dealing member.</p> <p>According to the information provided on the website of the CSCS, it has an agreement with all Nigerian banks to act as settlement banks for the settlement of the cash leg of trades through the Nigerian Inter-Bank Settlement System (NIBBS). The list of settlement banks on the CSCS website does not however seem to be up-to-date, since it includes some banks that have merged and some that are banks owned by the Asset Management Corporation of Nigeria (AMCON). All NSE dealing members maintain a trading account with one of the settlement banks to facilitate settlement of trades. In its operational guidelines, the CSCS requires NSE dealing members to fund their trading accounts in any one of the designated settlement banks before making a trade. This is designed to ensure that funds are available for the settlement of the cash leg of the transactions made on the NSE. If the dealing member fails to pay the transactions, the settlement bank is responsible for payments.</p> <p>The settlement banks have to inform the NSE and CSCS at the latest at 12:00 p.m. on T+2 of those dealing members that might not settle their trades on T+3. By 4:00 p.m. T+2 the CSCS also sends the final settlement advice on dealing members' net financial obligations to their settlement bank. By 9:00 a.m. T+3 dealing members/custodians and any high net worth individuals must have funded their accounts for day T transactions. At the latest 10:00 a.m. on T+3 NIBSS would inform CSCS on any settlement bank default. Inability of any settlement bank to settle trades would cause</p> |

those trades to be cancelled in the settlement system by the NSE on or before 12:00. Securities on the unsettled trades would be placed on hold/blocked at the close of business on T+3.

The CSCS has not set any limits on the value of transactions for the settlement of which a settlement bank is responsible. There are no collateral requirements. The SEC, NSE or CSCS do not have any general powers to take other appropriate action, such as to compel market participants carrying or controlling large positions to reduce their exposures. The CSCS can manage the risk in the securities side since the securities are blocked automatically when a transaction is made. In the cash side, it is dependent on the dealing member and settlement bank managing the risk of non-payment.

The above means that there are no automated mechanisms in place in the settlement system to monitor large exposures arising from the buyers' payment obligations. In case of a failure, the first step would be the cancellation of the trade and the blocking of the securities in the seller's account. The seller would be exposed to any market risk arising from change in price.

#### **Default procedures**

The trade guarantee fund was established by the NSE in conjunction with the CSCS. It is to further ensure cash settlement of stock exchange transactions. Currently, each dealing member makes a one-time contribution of ₦100,000 to the fund.

In case of default by a dealing member its settlement bank(s) would need to settle the default at T+3. All securities purchases of the defaulting dealing member made on day T would be allowed to settle and would be frozen on T+3 by the CSCS. The NSE/CSCS may cause the default amount to be debited to the trade guarantee fund by a letter to the affected bank(s) and the custodian of the fund. There is a maximum amount to be covered from the guarantee fund, but it is not available on the CSCS website.

Default accounts must be funded by 9:00 a.m. on T+4. The dealing member has to ensure that its settlement bank confirms payment to the CSCS by 10.00 a.m. on T+4. The securities would then be moved from the frozen account to the account of the appointed dealing member. At 11.00 a.m. the NSE/CSCS appointed dealing member would sell the securities. The CSCS would then advise the settlement banks of proceeds from the sale to replenish the guarantee fund as the proceeds come in. If there is a shortfall between the proceeds from the sale of securities and the amount debited to the guarantee fund, the defaulting dealing member has to pay the shortfall before returning to the market. In case of surplus from sales, the surplus is paid to the trade guarantee fund and the NSE and CSCS.

#### **Short selling**

Short selling has become possible at the NSE on September 18, 2012. The following rules on short selling are included in the rules of the NSE as approved by the SEC.

1. A listed security may be sold short at a price below the last sale price.
2. A dealing member may not accept a short sale order in any security from another person, or effect a short sale in any equity security for its own account, unless the dealing member has borrowed the security, or entered into a bona fide arrangement to borrow the security which will be delivered on the date of delivery.
3. Naked short selling is prohibited.
4. All orders for short sale must be marked short sale.

According to the oral information given by the NSE and CSCS, market makers are not required to follow the above rule, but they can borrow the securities after having entered into a trade, e.g., T+1. As such, providing exemptions to market makers is in line with the IOSCO Principle. On the other hand, the above rule seems to facilitate changing the system in the future in such a manner

|  |   |
|--|---|
|  | <p>that even other parties would not need to have borrowed the securities prior to effecting the short sale, because of the use of the word may instead of shall in the rules.</p> <p>There is no reporting regime that would provide timely short selling information to the market or to the SEC.</p>   |
| Assessment   | Partly Implemented  |
| Comments   | <p>As highlighted in Principle 37 of the IOSCO Methodology, an efficient and properly structured clearing and settlement process that is supervised and uses effective risk management tools is essential for the management of large exposures arising out of trading activities. The settlement system operated by the CSCS does not have any particular mechanisms in place to manage the risks arising from the cash leg of the transactions made, beyond relying on the ability of dealing members and ultimately settlement banks to settle the transaction on behalf of the client, where necessary, or resorting to the trade guarantee fund. Given the weak financial condition of many dealing members, and also settlement banks, the settlement system does not seem to be well equipped to manage the risks arising from large exposures in case of client failure. The manner of dealing with settlement failures (cancellation of trades) raises questions about the finality of transactions in the settlement system, which is however outside the scope of this assessment.</p> <p>At least at the initial stage, on the basis of the oral information provided by the NSE and CSCS, the potential risks arising from short selling appear to be well controlled through the ban on naked short selling and the requirement on other parties than market makers to borrow the securities before the short sale is affected. Given the existing risks in the settlement system, it is essential to ensure that any extension of the possibility to sell short the securities without having borrowed them beforehand beyond the approved market makers will not lead to additional risks in the settlement system.</p> |
| <b>Principles Relating to Clearing and Settlement</b>  |   |
| <b>Principle 38.</b> Securities settlement systems and central counterparties should be subject to regulatory and supervisory requirements that are designed to ensure that they are fair, effective and efficient and that they reduce systemic risk. |   |
| Description  |   |
| Assessment   | NA  |
| Comments   | Not assessed.   |