

PROTECTION OF INDIVIDUAL INVESTORS AT THE DAR ES  
SALAAM STOCK EXCHANGE: A CRITICAL ANALYSIS OF THE  
LAW.

A dissertation submitted in partial fulfillment of the requirements for the  
Award of the Masters Degree in Law of Mzumbe University,2013.

PROTECTION OF INDIVIDUAL INVESTORS AT THE DAR ES  
SALAAM STOCK EXCHANGE: A CRITICAL ANALYSIS OF THE  
LAW.

By

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CERTIFICATION

We, the undersigned, certify that we have read and hereby recommend for acceptance by Mzumbe University, a dissertation entitled **Protection of Individual Investors at the Dar es Salaam Stock Exchange; a critical analysis of the law**, in partial fulfillment of the requirements for award of Masters Degree in Commercial Law of Mzumbe University.

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**DECLARATION**

I, Laura George Sempeho, declare that this dissertation is my own original work and that it has not been presented and will not be presented to any other University for a similar or any other degree award.

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Moreover I would like to express my gratitude to Mr. Lawrence Sangawe, stock broker and Mr. Urio, Licensed Dealing Member (LDM) of Tanzania Securities, who without tiring, assisted me in my initial stages of my research and data collection.

## **DEDICATION**

This work is dedicated with love to my daughter Lunairis, who has been a great inspiration in my life.

## **ABBREVIATIONS AND ACRONYMS**

- DSE - The Dar es Salaam Stock Exchange.
- CMSA - The Capital Market and Securities Authority.
- ERP - Economic Recovery Programme.
- IFRS - International Financial Reporting Standards.
- ISAB - International Standards of Accounting Board.
- IOSCO - International Organization for Securities Commission.
- IPO - Initial Public Offer
- LDM - Licensed Dealing Members.
- MBA - Masters in Business Administration.
- NICOL - National Investment Company Limited.
- NMB - National Micro-finance Bank.
- OECD - Organization for Economic Co- operation and Development.
- ROSC - Report on Observance of Standards and Codes.
- SAP - Structural Adjustment Programme.
- UDSM - University of Dar es Salaam.

## **List of Statutes**

### **Principal legislation**

Companies Act [Cap 212 R.E.E2008]

The Capital Markets and Securities Act [Cap 79 R.E 2002]

### **Subsidiary legislation**

The Dar es Salaam Stock Exchange Blueprint

Capital Markets and Securities ( Establishment of Stock Exchange) Regulations, 1996

Capital Markets and Securities (Accounting and Financial Disclosure Requirements) Regulations, 1996

Capital Markets and Securities (Register of Interests in securities) Regulations, 1996

Capital Markets and Securities (Prospectus requirements) Regulations, 1997

Capital Markets and Securities (Advertisements) Regulations, 1997

Capital Markets and Securities (Conflict of Interest) Guidelines, 2002

Capital Markets and Securities (Guidelines on Corporate Governance) Guidelines, 2002

## **ABSTRACT**

This work is about the protection of individual investors at the Dar es Salaam Stock Exchange (DSE). The researcher focused on individual investor as a minority group, who invested less number of shares than institutional investors. The work aimed at checking the effectiveness of the laws and regulations at the Dar es Salaam Stock Exchange and how they guarantee investor protection. The research was conducted in Dar es Salaam city where the DSE and CMSA offices, the Securities brokerage firms and most of the individual investors are located.

The data was collected from DSE and CMSA legal departments through interviews of the officials. At the Securities Brokerage offices structured interviews were conducted to obtain primary data. Questionnaires were issued to Eighty (80) individual investors from different professions and specializations, five investors from each of the sixteen listed companies at DSE.

The researcher found that the laws on stock market guarantee investor protection but the major hindering factor is the application of the said laws on investors who do not have adequate awareness on their rights, on the prohibited practices, and even in reading the financial statements of the companies invested in. Further, the DSE and CMSA lack the adequate technology to detect the prohibited offences such as the insider dealing which limits the protection of the interests of investors.

The recommendations are to increase the awareness of the individual investor through the LDMs and brokers who deal with the investors on a day to day basis. There is also a need for improvement of technology to detect prohibited offences and facilitate in collection of evidence to prosecute offenders.

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## CHAPTER ONE

### INTRODUCTION AND BACKGROUND INFORMATION

#### Introduction

Trading of stocks and bonds in the secondary markets is carried out by the Dar es salaam Stock Exchange (DSE) in Tanzania; but general supervision of the stock markets is regulated by the Capital Markets and Securities Authority (CMSA), which is governed by the Capital Markets and Securities Act<sup>1</sup>.

The research work focused on small or individual investors. Individual investor here means a private person apart from a company or institution that invests in the listed companies of the DSE. Individual investors are those who buy or sell shares for their personal account, and not for a company or organization<sup>2</sup>.

This small and individual investors were specifically chosen, because they are less sophisticated in stocks investments compared to companies and institutions. The companies have experts to assist them in deciding which companies to invest in and for what gain. On the other hand, individual investors in most cases, enter into the stock market world with or without adequate knowledge of the functioning of the market other than obtaining dividends or the buying and selling of shares. However it is questionable whether such investors are aware of their rights against fraud or misappropriation by the licensed dealing members and brokers and the remedies available to the individual investors once such acts happen.

The main focus of the research was to assess whether the said individual investors are fully aware of the rights and how protection is ensured at the DSE as they carry on trade

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<sup>1</sup> Act No.5 1994

<sup>2</sup> Definition of Retail investor Retrieved on 22/04/2012 from World wide web <http://www.investopedia.com>

transactions in the market; and whether the enacted laws on capital markets do safeguard the interests of individual investors at the DSE.

Further the study considered whether the stock market itself operates according to the said laws.

### **1.1 Background to the problem**

The Stock Exchange is a place where secondary trading of securities takes place. Through Initial Public Offers (IPOs) is where shares and bonds are issued for the first time. Securities are documents of title that acknowledge the indebtedness and rights to proceeds in respect of which such documents are issued. Companies in need of funds can sell their shares and investors with excess funds invest in an anticipation of getting dividends or interests in future from companies that issued those securities.<sup>3</sup>

Stock exchange developed as part of financial reforms by the Government of the United Republic of Tanzania, through Structural Adjustment Programme (SAP) and Economic Recovery Programme (ERP) with the aim of liberating the economy, which was previously controlled by the Government to a capital market economy. Before this, the Government-owned financial institutions were the only source of finance<sup>4</sup>. Banks were the main financiers of companies since there were no collective schemes other than pension funds and insurance companies<sup>5</sup>. One of the financial sector reforms was the enactment of the Capital Market and Securities Act, 1994, which led to the establishment of the Capital Market and Securities Authority<sup>6</sup>. The Dar es Salaam Stock Exchange (DSE) was established under the Capital Markets and Securities Authority (CMSA) as an institution which dealt with the secondary trading of securities.

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<sup>3</sup> Rajab M. ; Factors affecting the development of Stock exchange in Tanzania; a dissertation submitted for the partial fulfillment of the requirement for the degree of Masters in Business Administration (Finance) at the University of Dar es Salaam, October 1996 p 1

<sup>4</sup> Rajab ibid.

<sup>5</sup> Kibola H; The regulation of the capital markets in Tanzania "Is there room for improvement?", DSE Journal , Issue no. 35, April 2008

<sup>6</sup> Section 10 of cap 79 R.E 2002.

Stock exchanges are normally established by the private sector; but since the Tanzanian private sector is lowly developed the CMSA had to establish it. The first company to be listed at the DSE was the Tanzania Oxygen Limited (TOL) followed by Tanzania Breweries Ltd (TBL); until October, 2012 there are seventeen listed companies.

The DSE lists shares and bonds, which provide companies, the Government and the Municipal Authority with a source of funds from both the public and institutional investors.

Investor protection is also guaranteed through corporate governance, where the activities of the companies existing in the capital market have to observe standards, which will safeguard the interests of the minority as well of those of majority shareholders in their day to day management. Through proper management of the companies, the shareholders will obtain the required benefits from their investments<sup>7</sup>.

This research work focuses on the effectiveness on individual investors protection under the regulations and rules of the DSE so as to ensure that the investors take part in a market, where there is full disclosure and transparency hence allowing the fair trading in the market. Attention was paid to issues related to fraud and misappropriation done by the licensed dealing members and brokers and remedies available to individual investors.

## **1.2 Statement of the problem**

The law on securities ensures that the stock market activities are regulated so that investor interests are protected. The investors invest their excess capital to enable the companies listed at the DSE to obtain funds to fulfill their financial obligations. Investors interests are protected by specific laws and regulations<sup>8</sup> against fraud, misappropriation, negligence and bad practices; ensuring against poor accounting and financial disclosure requirements in the market which will lowers the confidence of the investor in the

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<sup>7</sup> Capital Markets Guidelines on Corporate Governance, pg 4

<sup>8</sup>The Companies Act[Cap 212 R.E 2002]; The Capital Markets and Securities Act [Cap 79 R.E 2002] and its regulations; the DSE Blueprint

market. The law does not protect the investor from loss but rather from infringed rights. This is because taking a risk is part of the reward in investment activities.

The protection of investors in the stock market is guaranteed by the law<sup>9</sup> through disclosure to the investors of the financial details of the companies they are investing in, existence of qualified personnel who will advise the investors on issues of stock market that is the License Dealing Members (LDMs) and the brokers. Companies listed maintain the listing requirements that are set by the DSE under the authority of the CMSA<sup>10</sup>, Thus, in this aspect, the requirement of filing Annual Financial statements of the company according to International Financial Reporting Standards (IFRS) and the National Board of Accounting and Auditing (NBAA)<sup>11</sup>, helps investors make informed decisions after accessing the same. A good example is the National Investment Company Limited (NICOL), which had offered its shares at the NMB, without first providing its financial statement to its investors, and this led to the company being delisted in 2012. During this time NICOL was under investigation for non-compliance with the DSE requirement on financial disclosure whether the LDMs and brokers continued to trade in the said stock while knowing the same. The question is whether the interests of individual investors could have been safe-guarded before or after the company had been delisted. And what remedies do the individual investors have?

The law provides for protection of investors under the DSE, but is the said protection effective? Is the law followed to the letter so as to ensure that the rights of investors are not jeopardized?

This research looked into the provisions set in the DSE Blue print of 2003 as well as the Capital Market and Securities Act<sup>12</sup> and its regulations<sup>13</sup> on protection of individual investors.

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<sup>9</sup> *ibid*

<sup>10</sup> Rule 18 of the Capital Market and Securities (Establishment of Stock Exchanges) Regulations [Cap 79 R.E 2002]

<sup>11</sup> Rule 4.6 (g) of the DSE Blueprint.

<sup>12</sup> Cap 79 R.E 2002

### **1.3 Objective of the Research**

This work was guided by the following objectives;

#### **1.3.1 General Objective**

To determine the effectiveness of the DSE, in implementing its rules and regulations in safeguarding individual investors protection.

#### **1.3.2 Specific Objectives**

- a) To determine the extent of investors protection guaranteed by the DSE, when dealing with securities in the listed companies.
- b) To examine the extent of the benefits of investing in the listed companies of the DSE.
- c) To examine the extent legal reforms that meet the current needs of the stock market.
- d) To examine the extent of awareness provided by the LDMs and securities brokers in the market.

### **1.4 Hypothesis**

The hypothesis of this research undertaking was formulated as follows:

- The laws of Tanzania do not fully protect the interests of the investor in the stock market industry.
- The investors in Tanzania lack adequate awareness on the remedies available where there is infringement of their rights in the market.
- Lack of readily available remedies to aggrieved investors in the market.

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<sup>13</sup> Regulations made by the capital markets to enable the stock market to function more effectively.

### **1.5 Research Questions**

. The research work aimed at finding answers to the following research questions;

1. How are the investors protected at the stock market?
2. Does the existing law provide for effective protection of investors at the Stock Exchange?
3. Do the brokers and LDMs provide enough knowledge on individual investors as they enter to trade in the market?

### **1.6 Significance of the study.**

To determine the effective application of the stock market laws in ensuring and upholding individual investors interests in the stock exchange and make suggestions on any gaps in law that interfere with the protection of investors in the stock market.

### **1.7 Scope and limitation of the study**

The scope of this study limited to Dar es Salaam City, where the offices of DSE, CMSA and the LDMs and brokers are located . The laws that were the main focus of the work were limited to national and international laws on stock exchange.

### **1.8 Literature Review**

**Rajab**<sup>14</sup> in his work states that for protection of investors to be effected there must be anti-fraud laws protecting investors from fraud. Laws to protect the public from dishonest selling of financial products and some insider trading law raise the confidence in the market. He further states that in order to ensure continuous order flows from investors there is a need of transparency by the stock market in order for them to be informed as to what is happening in the market. In order for securities to be listed they must comply to listing requirements which ensure trading in securities is done in a fair, open and orderly

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<sup>14</sup> Rajab M. ., p 23, 24, 38 *op cit*

basis allowing the public unrestricted access to information so as to facilitate reasonable decisions with respect to investment in listed securities.

**Malima**<sup>15</sup> states that professionals in the stock exchange are under a duty to full disclosure to the investors since they are the ones who have full background knowledge of the companies listed at the DSE or else face consequences. Though he also observes that as much as strict application of the law is good for investor's protection but it may also cause rigidity of the market which is not good for business. He states that investors are protected through the Fidelity Fund, when compensation is needed for negligent acts of the experts and proper accounting is also another way.

**Lalika**<sup>16</sup> states that the Capital Market should make sure that all companies raising funds through it comply with all requirements in order to ensure investors are well informed on any terms concerning particular kind of security being offered in the market. He further writes that the Capital Market operates under conditions that all market participants have equal access to information due to transparency; which implies that there is honest and adequate timely disclosure of the financial information to the participants.

**Massinda and Komba**<sup>17</sup> argue that, one of the most effective investor protection is the requirement for full disclosure. The assumption is that full disclosure enables the investor to acquire all relevant information and therefore he can make informed decision on issues relating to the market.

**Kyaruzi**<sup>18</sup> merely mentions that investor's confidence is shaken by bankruptcy of the said listed companies and that the DSE provide strict conditions that a company must comply with before being listed. And measures that the stock market would take for

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<sup>15</sup> Malima B.( 2006); The liability of professionals in the Capital Market and Securities Act[Cap 79 R.E 2002] : Theory and Practice; Unpublished thesis, UDSM , p 45

<sup>16</sup> Lalika S.J (2000); Capital Markets in Tanzania. The DSE its problems and prospects; Paper submitted in partial fulfillment of the degree of LLM at the University of Dar es Salaam, p 27

<sup>17</sup> Massinda & Komba ; Disclosure requirements for collective investment schemes; Paper presented at the CMSA/TAA joint seminar for accountants and auditors at Karimjee Hall Dar es Salaam between 9<sup>th</sup> – 10<sup>th</sup> June, 2000.

<sup>18</sup> Kyaruzi D.(2006); the Factors affecting demand and supply of securities in Sub-Saharan Africa; the case study of securities listed at the DSE; unpublished thesis, UDSM

companies that seem not be performing well in the market such as encouraging mergers and acquisitions which is not favoured by most companies.

**Drake**<sup>19</sup> argues that regulation of the stock markets helps to control illegal acts such as fraud, manipulation and other dishonesties in the market. As much as such practices are difficult to police, he views it a way to control malpractice and hence encourage confidence among the investors in the market since their interests are secured.

**Pudensiana**<sup>20</sup> notes that regulations in the stock market should not be too strict to the point of hindering growth of the market. As much as there are many requirements to be fulfilled in order for a company to be listed, it should not be forgotten that a freer market is bound to flourish than a market full of restrictions hence affect the interests of the investors.

**Semzigi**<sup>21</sup> states that previously before the existence of a capital market most people used the banking sector, and now investors would only invest if they are guaranteed they can increase their holding quickly, conveniently, inexpensively and at the time of their choice by trading in the secondary market. Again the stock market has also helped governments find a source of income through issuance of bonds instead of the foreign loans and aid of the past. Furthermore, the capital market reform is supposed to encourage more investors to join the securities market.

**Norman**<sup>22</sup> writes that for a company to be listed it must have worthy qualifications in order to protect the interests of investors in the stock market. He further points out professional performance is also very essential in the carrying out of the same objective, since it is through the professionals that financial statements are made and the reputation

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<sup>19</sup> Drake J.P.(1985); "Some reflection on the problems affecting securities market"; Fin Africa Journal Vol. ix.

<sup>20</sup> John P.; Analysis of the factors that make companies reluctant to list in the Dar es Salaam stock exchange, MBA, UDSM, unpublished material, Nov. 2009

<sup>21</sup> Semzigi R., An Evaluation of Capital Market Reforms and Their Effects on the Development of Securities Market in Tanzania, MBA Dissertation, UDSM, Nov 2008

<sup>22</sup> Norman S.A, The role of the Dar es Salaam Stock Exchange in safe guarding securities investors in Tanzania; International Business Management, Medwell Journal; Faculty of MBA at Iringa University College, Tumaini University, 2010.

of the firm is built. He also touches on the Fidelity Fund as a means to compensate investors who have suffered loss for fraud and misappropriation of the acts of the Licensed Dealing Members negligence.

**Abayo**<sup>23</sup> researched on the listing requirements of the Dar es Salaam Stock Exchange, he observes that the Blueprint clearly advocates for investors protection even when they are a minority. He further discussed whether the law is observed on investor protection, in the stock market's daily activities.

**Kaduma**<sup>24</sup>, writes on the regulatory environment of the capital market and securities in Tanzania, he states that the regulatory statement comprises of the legal framework, objective of regulation and regulation of the securities market. His focus is on the Capital market and securities authority which is the supervisory body of the DSE; hence observing its activities further highlights the effectiveness of the DSE on investors protection.

**Dominic and Benedict**<sup>25</sup> have made a study on the development of the capital markets, with focus on the stock exchange market. The emphasis that development cannot be separated from law but rather work simultaneously. Therefore without proper regulation the stock market will not develop at all due to lack of order.

**Report on Observance of Standards and Codes (ROSC)**<sup>26</sup> states that the Capital Market and Securities Authority deals with regulation of all participants in the stock market from the entities that list their equities and debt are publically traded, the brokers,

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<sup>23</sup> Abayo A.G; Listing and Prospectus requirements in Tanzania. A paper at CMSA/TAA for Accountants and Auditors, Dar es Salaam, 9<sup>th</sup> January,2001.

<sup>24</sup> Kaduma J. ; Regulation of the Capital markets in Tanzania, CMSA workshop at Dar es Salaam, May 2006.

<sup>25</sup> Pius D. & Silvanus B., “Development of Capital Markets in Tanzania with an emphasis in Stock Exchange markets”, a study in law and development, a dissertation in partial fulfillment of the award of Degree at UDSM, June 1996, p 21-27

<sup>26</sup> Report on Observance of Standards and Codes(ROSC), Tanzania Accounting and Auditing, 2005, p 5

dealers, investment advisors and the DSE itself. He states that the CMSA provides for the disclosures of listed companies upon entering the market by providing annual financial statements as per the Tanzania Accounting standards and the NBAA provided for under the Capital Markets ( Accounting and Financial statements) Regulations of 1997. While the DSE provides for the continuous disclosure of the listed companies by providing annual financial statements that comply with International Accounting Standards (IFRS/IAS) under the DSE Blueprint, 2003.

**Burke**<sup>27</sup> in his journal differentiates between institutional investors and individual investors in the stock market. The former require regulation to ensure adequate capital reserves, to protect against fraud, and to prevent systemic failure of the financial system. The latter require protection to ensure that the markets provide a level playing field, to assure that market prices are not manipulated, but set by material information about listed companies, and to provide effective remedies against violations of trust and breach of market rules. Investor protection legislation is designed to induce retail investors to take risks. He further states that legal systems have adopted six generic approaches to protection of investors in financial markets which are, information disclosure, direct regulation of institutions, firms, brokers, and organized exchanges operating the markets, prevention of fraud, the law of private contract, investor insurance schemes, and sanctions for violations and enforcement. He concludes thus the delivery of prospectuses, proxy statements, and annual reports, though important, do not serve the needs of the retail investor, as the latter lack the skills required to draw conclusions from these documents to make informed investment decisions.

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<sup>27</sup><http://elaw.murdoch.edu.au/index.php/elawmurdoch/article/viewFile/38/13> Accessed on 26/08/2012 at 6:30 pm

John JA Burke 'Re-examining Investor Protection in Europe and the US'; eLaw Journal: Murdoch University Electronic Journal of Law (2009) at pp 6-33

**Leuz** et al,<sup>28</sup> argue that investor protection plays an important role in influencing international difference in corporate management. That strong and well enforced outsiders rights limit insiders acquisition of private control benefits, and consequently, mitigate insiders incentives to manage accounting earnings because they have little to conceal from the outsiders i.e investors. Their insight suggests that the pervasiveness of earnings management is increasing in private control benefits and decreasing in outside investor protection. Earnings management is the alteration of firm's reported economic performance by insiders to either mislead some stakeholders or to influence contractual outcome. Insiders, such as controlling owners or managers, can use their control over the firm to benefit themselves at the expense of stakeholders. This means that some value is enjoyed exclusively by insiders and thus not shared with non-controlling outsiders. For example, insiders can use their financial reporting discretion to overstate earnings and conceal losses that would prompt outsiders interference. Insiders can also use their accounting discretion to understate earnings at times where company has had good performance with an aim of creating reserves for future period. Investors rights can be safeguarded laws which reduce the need for insiders to conceal their activities, this can be done by replacement of management as a disciplinary action. They further state, earnings management to be more pervasive in countries where legal protection of investors is weak.

Most of the researchers provide for the ways in which investors can be safeguarded and their interests protected which is through disclosure. But do not deal with the legal protection of the said investors in the market once their rights are infringed, the remedies available to individual investors upon suffering from loss fraudulent Acts of the licensed dealing members and the brokers.

Therefore this research work intended to check in detail the protection of the investors from the assessment of law provisions relating to listed stock at the DSE.

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<sup>28</sup> Leuz C. et al; Earnings management and Investor protection and International Comparison; Journal of Economics 69 (2003) 505-527

## **1.9 Research Methodology**

### **1.9.1 Data Collection**

The essence of the methodology is to work as a matter of necessity to come up with valid and reliable findings. Both primary and secondary data were used. Primary data was collected through interviews and structured questionnaires. Unstructured interview was used through asking questions depending on the response of the interviewee. This method was chosen because it facilitates the collection of relevant information and obtain more clarity to unclear answers through asking of more questions.

Structured closed ended questionnaires were issued to individual investors, since their number is too great for an interview method to be effective with concerns of time and resources available. The questionnaires were issued to the respondents by post and some physically at the securities brokerage offices.

Secondary data was obtained from reading books, journals, thesis and dissertations on the subject done by others. At the early stages of the research the researcher visited the University of Dar es Salaam library because it has a large number of dissertations and thesis so as to go through work done by other researchers on the matter of investors' protection at the DSE. Moreover, internet surfing assisted in obtaining articles, journals and thesis done by researchers in other jurisdictions to obtain their views on investor protection in their countries so as to make analysis and learn new ideas that can improve our stock market situation.

The researcher further visited the CMSA and DSE offices, where unstructured interviews were conducted with the officials there so as to determine the extent of investor protection at DSE, with critical analysis on the law. Here pamphlets, brochures, booklets and other documents were provided in order to further the research. Moreover, brokerage offices were also visited since they are the ones who deal directly with investors in sale and buying of securities. Here structured interview was conducted, where a well laid out list of questions was used to obtain the data needed.

Again, the researcher issued questionnaires to the individual investors so as establish whether the investors take on protection at the DSE, and whether they were aware of the rights as investors and measures to be taken once aggrieved.

### **1.9.2 Research Design**

A research design is a plan that a researcher sets out in order for the research work to go on smoothly from start to finish, with a view of saving time and finances but also ensuring obtain the best research work. The research design was descriptive research design since the researcher intends to get unbiased data which is also reliable.

Descriptive research design is appropriate for this research since it facilitates the determination of the characteristics of variables in the research; the way the law protects the rights and interests of individual investors in the stock market specifically at the DSE. The researcher analyzed the effectiveness of the laws under the DSE and CMSA on protection of individual investors.

### **1.9.3 Sampling Technique**

The sampling technique was non-probability sampling since the researcher selected the sample according to the needs of the research questions to be answered. Here the researcher deliberately picked the relevant sample from a population.

The DSE and CMSA head offices, the seven LDMS and brokerage offices as members of DSE. These were part of the sample since they are the authorities that deal with regulating, trading and buying and selling of shares at the stock exchange at the stock market respectively.

The five individual investors were selected by non-probability sampling from the seventeen companies listed at the DSE except African Barrick Gold which is cross listed and is yet to trade in at the market since its Initial Public Offer (IPO) was done in Britain.

The research focused on the DSE which is the sole stock exchange in Tanzania. The individual investors were five from each of the seventeen listed companies at the DSE, which makes a total number of eighty (80) investors as a whole. The researcher selected such number from each company so as to obtain an objective outcome of the research under study since some of the companies listed are doing well and some not. The CMSA and DSE offices were visited to obtain data. The researcher worked with their respective legal departments. The seven LDMs and the brokerage firms were also provide further details on the study.

#### **1.9.4 Analysis**

The research work used qualitative method of data analysis in order to determine the effectiveness of the laws in stock exchange in protection of investors from the data obtained. Qualitative analysis of data is most appropriate since the research's focus is centered on the effectiveness of the law in protecting individual investors at the stock market. The researcher would base on quantitative on evaluating the questionnaires handed out to the individual investors of the listed companies at the DSE, their analysis was graded in percentage and displayed the same by use of pie charts in determining the number of investors is aware of their rights and those have ever had any problems as they traded their shares at the stock exchange.

## **CHAPTER TWO**

### **LEGAL FRAMEWORK ON INVESTOR PROTECTION**

#### **2.1 Introduction**

Investor protection is one of the main objectives of the securities markets in the world. In order for the market to function effectively the investors' must be safeguarded against fraud and other practices which will interfere with their investments hence causing them to suffer loss. Protection of investors will instill confidence in the stock industry; hence more investors will be willing to invest their funds in stocks. Further investor protection will ensure the integrity of the market.

Investor protection can be looked at from the different of angles such as establishment of a regulatory body to regulate the securities business, placement of controls over the activities of market intermediaries, prohibition of practices that conflict with legitimate interests of the investors, investor protection schemes and disclosure requirements in respect of issuers of securities.

#### **2.2 Regulatory Bodies of the Securities Market**

The Capital Markets and Securities Authority (CMSA) was established pursuant to

Act No. 5 of 1994 for the purpose of promoting and facilitating the development of an orderly, fair and efficient securities market in Tanzania. This is the body that licenses market participants and makes approval of stock exchanges and supervises the activities in the securities market.

The DSE is a body corporate which deals in trading of listed securities in Tanzania. It was established in 1996<sup>29</sup> as an initiative made by the government to transform the economy from public sector bias. It became operational in 1997 as a stock exchange<sup>30</sup>.

Both bodies of which the CMSA is the leading authority deal with the control and supervision of the trading of listed securities in the country. The CMSA supervises all the activities done by DSE and calls into question any act that does not seem to comply with the regulations and rules under CMSA such as the CMSA Act and its regulations and the Companies Act<sup>31</sup>.

In year 2000, the CMSA introduced a regulation on capitalization and rights issues regulation. These regulations have in one or another aim at protecting the interests of investors at different levels from listing of the companies at the Dar es Salaam Stock Exchange (DSE, issuing of their prospectuses to the investor actually buying and selling of the shares at the brokers' offices to the trading act by the LDMs at the DSE to the authority supervising capital markets in the country.

Mdami<sup>32</sup>, her study checks on the market efficiency of the DSE by considering extent and quality of disclosure in the market specifically the timing and the quality of information provided; price reaction once dividends are announced and when paid up; where earnings of the companies are announced and further checking the extent of involvement of registered dealers and brokers in influencing the market efficiency. She deduces that

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<sup>29</sup> Norman S.A; The role of the Dar es Salaam Stock Exchange in safe guarding securities investors in Tanzania; International Business Management, Medwell Journal; Faculty of MBA at Iringa University College, Tumaini University, 2010 p 222

<sup>30</sup> Kibola H.S, **The Regulation of Capital Markets in Tanzania**; Is there room for Improvement?; DSE Journal, Issue No. 35, April 2008 p 10

<sup>31</sup> Cap 212 R.E 2002

<sup>32</sup> Mdami C. (2006); An assessment of market efficiency in emerging stock exchange: case study of DSE; MBA ( Finance)unpublished dissertation UDSM pp 11-12

investors react on the price of shares depending on the information obtained about the company, the higher the dividend the higher the price of shares hence considered DSE not to be so efficient.

### **2.3 Investor protection Schemes**

There several ways of protecting investors in stock and securities markets. These are Fidelity Fund and dealers' deposit. The Fidelity Fund is maintained by a stock exchange and administered by its council<sup>33</sup>. The Fund is made from moneys from member companies, interests and profits from investment of funds and any other moneys paid into it. The aim of establishing the Fund is to settle claims against DSE, to also settle legal and other expenses incurred in investigating or defending a claim. The major use of the Fund is to compensate persons who suffer pecuniary loss from fraudulent or dishonest securities dealing by licensed dealing member of DSE.

Another means of investor compensation scheme is a dealer's deposit. This is a deposit of Tshs. 100,000/= (one hundred thousand shillings)<sup>34</sup> or more made by the dealer upon gaining acceptance for a license.

These compensation schemes were set up for the right purpose but they deem useless since for example, since the establishment of the Fidelity Fund to date it has never been used to compensate a single investor who is aggrieved from loss due to negligence of the LDM; this is due to the conditions that an investor must comply to in order for the DSE Council to accept an application for Compensation.

It is provided for under the DSE Blueprint<sup>35</sup>, that an investor with a claim that is subject to be compensated by insurance or any other compensation claim, then the Council shall postpone its decision in relation to a claim until the amount payable is determined by the other scheme. The Council further may reject a compensation claim if the investor did in

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<sup>33</sup> Section 83 of Capital Markets and Securities Act [Cap 79 R.E 2002]

<sup>34</sup> DSE Handbook 2010 p 15

<sup>35</sup> Chapter 9, paragraph 7.5

anyway contribute to the loss incurred. Moreover, any irregularities in the application for compensation done by the aggrieved investor may lead to rejection of his claim.

Moreover, there is a dealer's guarantee in which LDM before admission to the stock exchange as an applicant is required to provide a bank guarantee as a security for the possibility of default on his part. This provides an avenue to control default on the part of LDMs.

It is obvious from these provisions that priority is not given to the aggrieved investor but to the DSE so as to be able to retain the funds set up in the Fidelity fund even though the investor is truly aggrieved.

The DSE Blueprint further provides that;

*The amount which may be paid out to an investor shall be 80% in respect of all claims which have been made by the investor subject to a maximum of ... provided that the compensation paid from the Fund in any one year shall not exceed 50% of the balance available in the Fund<sup>36</sup>.*

This provision does not favour the aggrieved investor due to loss suffered but intends to safeguard the DSE's Fidelity Fund from being depleted. The current amount of compensation shall not exceed a hundred thousand shillings (Tshs. 100,000/=)<sup>37</sup> for a claim. The figure is unrealistic since an investor may lose more money the set amount, hence discouraging big investments since there is no proper method of compensating those who lose a lot of money due to LDM negligence and misappropriation.

## **2.4 Disclosures by issuers of securities**

Issuers here are the companies that want to issue their shares to the public. No company may issue shares without the authorization of the CMSA. The issuing company must prepare a prospectus which must be approved by the CMSA;<sup>38</sup> checking whether the

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<sup>36</sup> Chapter 9, para. 7.6

<sup>37</sup> The said figure was obtain from interviews conducted by the researcher at the DSE, CMSA and securities brokerage firms.

<sup>38</sup> Rule 5 of the Capital Markets and Securities (Prospectus Requirement) Regulations [Cap 79 R.E 2002]

prospectus has relevant information which will assist a prospective investor to make an informed assessment of the financial position of the company its assets and liabilities and rights attached to the securities that are being offered, which is further provided under section 132<sup>39</sup>;

*The Authority shall not approve a prospectus unless –*

*(a) It contains all such information as investors and their professional advisers would reasonably require, and reasonably expect to find there for the purpose of making an informed decision...*

If the issuer does not provide the relevant information as required by law, any loss suffered by the investor due to omission or misleading statements shall be borne by the Directors of the Company to compensate the investor, this provided for under section 49(1) of the Companies Act<sup>40</sup> which states as follows;

*...where an offer document invites persons to acquire shares in or debentures of a company, the following persons shall be liable to pay compensation to all persons who acquire any shares or debentures in reliance on offer document for loss or damage they may have sustained by reason of any untrue statements included there in-*

*(b) every person who is a director of the company or, as the case may be...*

There are two CMSA regulations that closely deal with investor protection in the securities market which focus on the prospectus requirements and guidelines on corporate governance. Below is the discussion of each both regulations and their contribution on investor protection at the stock market;

#### **2.4.1 Capital Markets and Securities (Prospectus requirements) Regulations, 1997**

A prospectus is a document made before securities are offered to the public. It is a mandatory requirement which enables the investors to be informed of the capabilities of the company before one decides to invest. The regulations provide for the format of the prospectus which must state the rights of shareholders, information on bankers, the

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<sup>39</sup> Cap 79 R.E 2002

<sup>40</sup> Companies Act, 2002

capital the issuer has, debt of the issuing any material contracts, the use of the proceeds from the issue.

A prospectus must state the rights the prospective and current shareholders of the company enjoy by virtue of investing in the company. It must clearly state the right to dividends, right to subscribe to new shares, right of redemption, voting rights of the shareholders. This is one of the most important provisions.

Another important provision is the on the information of directors of a company, it must be stated clearly if any director has ever been a director in another company which has been declared bankrupt

*.....(1) if a person who has been declared bankrupt or insolvent by a competent court in Tanzania or elsewhere and has not received his discharge acts as a director of, or directly or indirectly takes part in or is concerned in the management of, any body corporate except with the leave of the court, he shall be liable for conviction to imprisonment or to fine or to both...<sup>41</sup>*

or has convicted and temporarily or permanently prohibited from acting as an investment adviser or a director

*...(1) Where-*

*(a) A person is convicted of any offence in connection with the promotion, formation or management of a company or  
.....the court may make disqualification order against a person providing that he shall not, without leave of the court, be a director of or in any way, whether directly or indirectly, be concerned or take part in the management of a company for such period not exceeding fifteen years....<sup>42</sup>.*

This aims at making sure that a director who had gone through such proceedings not to tarnish the image of the soon to be share issuing company for bad management due to the poor background of the director.

The CMSA under this regulation has set out the format for a prospectus of which if there exists any irregularities one must amend the prospectus with the direction of the CMSA<sup>43</sup>.

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<sup>41</sup> Section 196(1) of Companies Act, 2002

<sup>42</sup> Section 197(1) ibid

<sup>43</sup> Regulation 4 of the Capital Market and Securities ( Prospectus requirements) regulations

This aims at protecting the investors, who rely on the information put there to decide whether to invest or not.

#### **2.4.2 Capital Markets and Securities (Guidelines on Corporate Governance) Guidelines, 2002**

The aim of the guidelines is to promote capital market growth through improvement of corporate performance, capital formation and maximization of shareholder's value as well as protection of investor's rights in the public listed companies. The said guidelines are in line with international standards as of those of Organization for Economic Cooperation and Development (OECD) principles of corporate governance.

The corporate governance entail that shareholders must participate in the decision making of the company since will affect their interests such as major disposal of company's assets, restructuring, takeovers, mergers, acquisitions or reorganization.

On the matters of audits and accounts, the board is under a duty to present financial details in the most understood able way so that the investors may be aware of the status of the company. Further there should be a sound financial system which safe guard the interests of the investors in their investments and assets.

The guidelines further provide for the protection of the rights of minority shareholders from those of majority shareholders, that each group must be treated equally. Every shareholder shall be entitled to distributed profit in form of dividends and other rights for bonus, shares, script, dividend or rights issue, as applicable and in the proportion of its shareholding in the company's share capital.

A public listed company must prepare briefings half-yearly or annually or whenever necessary to the investors so that they can be informed on the performance of the company; this will promote interactions with the investors and the company.

Massinda and Komba<sup>44</sup>, in their work argue that for protection of investors to be effective full disclosure is a requirement. With full disclosure the investor shall have access to relevant information which will enable him to make an informed decision.

Burke<sup>45</sup>, in his article discusses about disclosure to a retail investor who in this context is an individual investor. It is considered full disclosure once the investor is provided with a prospectus of an issuing company to read about the details of the company he is about to invest in. An investor most times is not able to analyze the information in the prospectus without having the skill to understand financial statements, hence has to be helped with investment advisors or brokers. This makes investor protection dubious because the investor has to put all his faith in the professional who at times are not honest.

*...The retail investor then is left to rely upon professional advice or make conservative investments based on intuition and not necessarily in the best long run interest of the investor. In short, information asymmetry refers to the client's limited knowledge vis-à-vis the intermediary with regard to investment activity, information pertinent to evaluating the investment product, and the intermediary's self-interest in financial gain from client' activity<sup>46</sup> ...*

## **2.5 Control of market intermediaries**

Market intermediaries are the key specialists operating the capital markets; they are the parties who facilitate transactions in between issuers and investors on the primary market and between investors and investors on the secondary market. These are brokers, dealers,

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<sup>44</sup> Massinda & Komba ; Disclosure requirements for collective investment schemes; Paper presented at the CMSA/TAA joint seminar for accountants and auditors at Karimjee Hall Dar es Salaam between 9<sup>th</sup> – 10<sup>th</sup> June, 2000.

<sup>45</sup> John JA Burke 'Re-examining Investor Protection in Europe and the US'; eLaw Journal: Murdoch University Electronic Journal of Law (2009)

<sup>46</sup> Ibid p 9

authorized dealers representatives, investment advisors, issuance advisors such as legal advisor, reporting accountant, receiving and collecting bank.

The observance of ethics and professional conduct by market intermediaries is essential for market integrity and promotion of investor confidence. It is necessary therefore for all licensed market intermediaries be subjected to a code of conduct that promotes high standards of commercial honour observe security laws and regulations, encourage self discipline among members and foster just and equitable principles of trade.

The control of market intermediaries may be done by control of the use of the client's funds by following the instructions of the client to the latter; and that the funds must be held in a bank account in trust.

A dealer is allowed to trade in his accounts, but priority is to be given to the orders made by a client and his comes after, this can be guaranteed by timing the client's orders upon entering a dealer's office.

The CMSA has two regulations which facilitate the control of market intermediaries, these are regulations and register of interests in the market by members of CMSA and conflict of interest guidelines by CMSA members and employees.

### **2.5.1 Capital Markets and Securities (Register of Interests in securities)**

#### **Regulations 1996**

These regulations state that a register must be maintained keeping records of the securities in which members of staff of CMSA and other related have interest in. this helps to the CMSA to trace the said transactions hence allowing transparency which will curb the problem of insider trading.

Further a licensed dealer, dealer's representatives, investment adviser, investment representatives and financial journalists are required to maintain a register of securities he

has interest in<sup>47</sup>. The registration must be done within twenty four hours of acquisition or disposal of the interests.

### **2.5. 2 Capital Markets and Securities (Conflict of Interest) Guidelines, 2002**

The guidelines set out rules for the protection of members of CMSA and employees from conflict of interest, in matters relating to the market. The guidelines aim at preventing the likelihood that CMSA regulatory decisions are influenced by personal interests. Or the presumption that CMSA member and employees investment decisions are subject to insider trading.

Members of the Authority and staff of the CMSA must not exploit or appear to exploit to their personal advantage any information to which they may become privy as a consequence of their employment. This principle entails that insider trading is unlawful since it would give the members and employees more advantage than the other investors when it comes to deciding where to invest and when. Section 112 of the CMS Act<sup>48</sup> provide that, if any insider is to use such privileged information will have committed an offence.

### **2.5.3 DSE Blueprint**

In order for the DSE to insure that the investors interests are safeguarded it has set strict conditions as for the admission of a licensed dealing member (LDM) as member of the stock market. He must possess a valid dealer or broker's license, must also be admitted as an associate member of the stock exchange in accordance with the articles and must meet other qualifications set out by the DSE Council<sup>49</sup>. This means for one to become an LDM, he/she must be proven to be qualified by both the DSE and the CMSA.

Upon receiving the client's/investor's money the LDM is under obligation to establish a Trust Account so as to deposit the client's money for the purchase of securities and effect payment for securities transacted. The DSE shall have the authority to inspect such Trust

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<sup>47</sup> Rule 3 of the Capital Markets and securities (Register of Interests in Securities) regulations

<sup>48</sup> Cap 79 R.E 2002

<sup>49</sup> Chapter 3, paragraph 3.2 of the DSE Blueprint

Account whenever deemed necessary by its Council<sup>50</sup>. Here the DSE will be able to observe the transactions of the account hence protecting the client's money from misuse by the LDM. The LDM is allowed to withdraw his commissions and charges arising from the transactions sanctioned by the client.

The LDMs have a fiduciary duty to their clients and must also disclose any conflict of interest between the LDM and client must be disclosed and that the LDM may withdraw from representing the client<sup>51</sup>.

Malima<sup>52</sup>, refers to the intermediaries such as brokers and LDM to be agents or experts who know the history of the listed companies and are under a duty to inform all the necessary details to a prospective investor from the prospectus of the issuing company, which is highlighted under section 132<sup>53</sup>; this is because investor is not aware as to whether the information he has is truthful or not hence the experts are left with the task of defining the same to the investor.

## **2.6 Prohibited practices at DSE**

Practices prohibited by law that interfere with the rights of the investors and lead to loss of confidence in the market by the said investors due to suffering of loss caused by such predatory practices such as insider dealing/trading, market rigging, short selling, price manipulation.

### **2.6.1 Churning**

Churning occurs when a broker engages in excessive buying and selling of securities in a customer's account chiefly to generate commissions that benefit the broker. For churning to occur, the broker must exercise control over the investment decisions in the customer's

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<sup>50</sup> Section 69 of Cap 79 R.E 2002 and Chapter 3 paragraph 3.54 of the DSE Blueprint

<sup>51</sup> Chapter 3, paragraph 3.61 of the DSE Blueprint

<sup>52</sup> Malima B (2007); the Liability of Professional in the capital markets under the Capital Market and securities Act [CAP 79 R.E 2002]; unpublished LL.M thesis 2006/2007

<sup>53</sup> *ibid*

account, such as through a formal written discretionary agreement. The said purchases and sales do not in the end benefit the customer's investment objectives.

The effect of churning is the loss of money in the investor's account which will be due to the frequent sale and purchase of shares and the commissions charged by the broker.

### **2.6.2 Market rigging.**

An exchange operation by which the price of a security is artificially induced to rise or fall<sup>1</sup>. An illegal act or practice in which a person or company causes a price to be more favorable to an investor than market forces really justify. Rigged markets exist in order to attract investors to a company or project, but it is often not sustainable and in any case deceives the investor<sup>1</sup>. Any person who carries out the same is guilty of an offence<sup>1</sup>.

### **2.6.3 False Trading**

It is the practice of which is calculated to create a false or misleading appearance of active trading in any securities on a stock exchange or a false or misleading appearance with respect to the market for the price of any securities<sup>1</sup>.

### **2.6.4 Market Manipulation**

It is the carrying out directly or indirectly of two or more transactions in securities of a body corporate, in which transactions have or are likely to have the effect of raising, lowering, maintaining or stabilizing the price of securities of the body corporate in stock exchange aiming at inducing investors to sell, buy or subscribe for shares of that body corporate. For example, where a party places large numbers of buy orders to create an impression that there is buying interest, whereas in reality they will be cancelled and not executed, constitute an interference with the free operation of the market. This may mislead the public and make more investor want to invest thinking the stocks of the said company are good due high number of purchase hence manipulation.

### **2.6.5 Insider dealing**

It involves dealings in securities by persons who by their association with a body corporate are in possession of confidential information that is not yet publicly available but which may affect the prices of the shares released.

Inside information is the information that relates to the securities themselves or to the state of the company which issued them. The information must be specific and not have been made public and must be sort of information which, if it had been made public, would likely to have had significant effect on the price of those securities.<sup>54</sup>

Information becomes public when it is disclosed, for example, in a company press release or a widely read financial review. Information disclosed solely to person attending a briefing, the chairman of the company and professionals is considered not public. Existence of rumours alone is not sufficient to make information about a improvement in a company's financial situation could influence the price of its stocks.

Therefore the law prohibits a person from a proceeding six months who had specific dealings with a body corporate not to deal with any securities which may materially affect the price of those securities.

The above discussed prohibited practices in the market are well laid out even in the legislation but the biggest problem is the ability of DSE and CMSA to detect the same offences due lack proper technology. Therefore claims go unresolved due to lack of enough evidence to settle the same; this lowers the confidence of investors in the market.

### **2.7 Financial accounting disclosure**

The accounting function is an important aspect in the securities business because it serves as a systemic insurer against acts of fraud or loss of funds through negligent acts. Part VII of the Capital Markets and Securities Act<sup>55</sup> provides for Accounts and Audit with focus on the dealers and brokers handling of investor's funds.

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<sup>54</sup> Keenan & Riches; Business Law; Ninth Edition, 2009 p374.

<sup>55</sup> Cap 79 R.E 2002

Under the Capital Markets and Securities (Accounting and Financial Disclosure Requirements) Regulations, 1996, provide for the requirement of maintain accounting records and also the preparation of interim and annual financial statements. This will enable the CMSA and DSE to follow up easily on the performance of the company and how well the investors are benefiting from its activities.

This is a good method of keeping the investors informed but majority of individual investors do not have the ability to read and understand the financial information provided by the invested company hence end up relying on the interpretation from brokers and dealers which may be biased at times.

The regulations further provides for the keeping of customers' money in a Trust account by brokers. This will also help to manage the money and avoid the abuse of customers' funds before or after sale.

## **2.8 Conclusion**

From the discussion in this chapter it is apparent that investor protection is not fully guaranteed by the DSE despite its effort to do the same. This has been evident on the matter of compensation from the Fidelity Fund which is not adequate; difficulty in apprehending financial details which enlighten the investor on the activities of his investing company. Again there is lack of proper technology to detect prohibited practices in the market such as insider dealing, churning, market manipulation. Further research was conducted to determine the real situation in the current securities market

## **CHAPTER THREE**

### **THE SECURITIES MARKET AUTHORITY**

#### **3.1 Introduction**

Protection of Investors at the Dar es Salaam Stock Exchange (DSE) shall not be effected without the existence of the Stock Market regulatory Authorities; the Capital markets and Securities Authority (CMSA) and the Dar es Salaam Stock Exchange itself. This chapter highlights the way in which these two bodies with the assistance of International and Regional Commissions<sup>56</sup> to regulate the stock market in the country.

The CMSA is a supervisory body of the securities market in the country which under its law, the Capital Markets and Securities Act<sup>57</sup> empowers it to authorize the establishment of stock exchange of which the only existing is the DSE where stocks and bonds of listed companies must obtain authorization before offering the same to the public.

#### **3.2 The Capital Market and Securities Authority**

The Capital Markets and Securities Authority was established in 1995 under the Capital markets and Securities Act, Act No. 5 of 1994 as amended by Act No. 7 of 1997. The CMSA was established as part of financial sector reforms in the early 1990s which aimed at developing capital markets as a means of mobilizing long term savings and ensuring their efficient allocation to productive sectors so as to facilitate economic growth.

One of its major functions provided under section 10 of the Act<sup>58</sup> is surveillance of over dealings in securities, license market participants, and formulate principles for guidance

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<sup>56</sup> The International Organization of Securities Commissions (IOSCO) and the East African Securities Regulatory Authority (EASRA)

<sup>57</sup> Cap 79 R.E 2002

<sup>58</sup> Cap 79 R.E 2002

of the industry and protection of its investors' interests and integrity of the securities market against any abuses as well as advising the government on policies and all matters relating to the securities business.

### **3.2.1 Composition of the Authority**

The CMSA has a Board of Directors which governs the activities of the Authority. The Authority is composed of ten members in its Board established under section 6 subsection 3 of the Act.<sup>59</sup> It has a Chairman appointed by the President on the recommendation of the Minister of Finance, the Permanent secretary to the Treasury, the Governor of the Bank of Tanzania, the Registrar of Companies, the Attorney General, the Chief Executive Officer of the Authority and the remaining four members shall be appointed by virtue of their relevant experience in finance, economics, accountancy and law.

The Chief Executive Officer is responsible for the day to day activities of the Authority. The CEO is assisted by three directors who are in charge of Research, Policy and Planning; Market Development and Supervision and the Legal Affairs and Enforcement. There also six managers who assist in management of the Authority's activities under the Directors. The managers provide assistance in areas of finance, human resources, internal audit, legal affairs, market supervision and market development.

### **3.2.2 Powers of the Authority**

The functions of the CMSA are laid down under section 10 of the Act<sup>60</sup> which are to develop and promote the capital markets in the country, to issue license to market players such as the brokers,<sup>61</sup> dealers and agents, investment advisors and authorized dealer's representative. It also provides the approval for the establishment of a stock exchange<sup>62</sup>,

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<sup>59</sup> *ibid*

<sup>60</sup> *ibid*

<sup>61</sup> Section 32 of Act No. 4 of 1997

<sup>62</sup> Section 26 *ibid*

prohibiting trade in particular securities,<sup>63</sup> to restrain individuals from engaging in activities which constitute contraventions of the Act,<sup>64</sup> and to regulate the conduct of business and require disclosure of certain information.<sup>65</sup>

### **3.3 The Dar es Salaam Stock Exchange**

The DSE is the only stock exchange in Tanzania. The Exchange was incorporated in September, 1996 as a company limited by guarantee without a share capital. It became operational in April 1998. The DSE is therefore a non-profit making body created to facilitate the Government implementation of economic reforms and in the future to encourage wider share ownership of privatized and all the companies in Tanzania.

#### **3.3.1 The governing body of DSE**

The DSE is governed by a Governing Council, which consists of ten members drawn from various interested groups in the society. It is composed of three licensed dealing members, one associate member representing the institutional investors, two associate members representing the public and chief executive officer is an ex-officio member.

A member serves a term of three year and members are allowed to serve for a term of two consecutive terms, which makes a total of maximum six years.

The Council has power to appoint the top management of the Exchange and setting up of guidelines rules to be observed by members and those who obtain services from the DSE; such rules are listing rules, trading rules, clearing and settlement rules.

#### **3.3.2 Functions of the DSE**

The DSE plays the following functions in the capital markets industry, as provided for under the DSE Blueprint<sup>66</sup>;

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<sup>63</sup> Section 31(1) ibid

<sup>64</sup> Section 131(1) ibid

<sup>65</sup> Section 30 ibid

<sup>66</sup> Chapter Two, DSE Blueprint

One, the exchange provides a platform for raising capital for companies that need it through selling of securities to the public. This is through transfer of funds from Surplus Spending Units (SSU) to Deficit Spending Units (DSU). The DSU are usually institutions and individuals specifically the government and business firms, who need funds while the SSU are institutions and individuals who have access funds and transfer it to the DSU with a view of obtaining financial gain.

Two, the mobilization of savings for investment. Most individuals put their surplus capital in bank deposits where the interests are very small, but through the DSE there is a chance of mobilizing the funds that would have otherwise have been in banks into investments in hence promotion of industry and commerce.

Three, the stock exchange helps in redistribution of wealth by involving individuals in sharing profit in companies that had been formed by others. This will help to lessen the income inequalities in the society through dealing in securities.

Four, the stock exchange helps to improve corporate governance of companies. This is because there is a need to improve the management of the listed companies so that the shareholders may benefit from the efficiency of the company they have invested in.

Five, the stock exchange provides small investors with an opportunity to invest since such investments depends with the savings one has. This is because most investments require large capital of which only a few can take part in, but the DSE has included both small and big investors where one benefits as per his/her investment.

Six, the DSE provides a platform for the collection of funds to lend the Government or Municipal councils. This is done through offering of Bonds to the public where they are bought. Such funds are usually used in the roads constructions, housing estate, water treatment works and sewerage.

### **3.3.3 The Objectives of the Securities Regulation**

These objectives are set out under the International Organization of Securities Commissions (IOSCO) is recognized as the international standard setter for securities markets. Its membership regulates more than 95% of the world's securities markets and it is the primary international cooperative forum for securities market regulatory agencies. IOSCO members are drawn from, and regulate, over 100 jurisdictions and its membership continues to grow<sup>67</sup>. The objectives set out by IOSCO are three which are investors' protection, ensuring that markets are fair, efficient and transparent and reduction of systemic risks.

#### **3.3.3.1 Protection of Investors.**

The investors are the key players in the securities market; it is from their funds that companies obtain capital through shares in the said companies to carry out further investments of the said companies listed at the Dar es Salaam Stock Exchange. Investors should be protected from deceit, manipulation and fraudulent practices which may cause them unnecessary loss. Practices such as insider dealing, front running, market rigging and short selling. Again disclosure of information is another way for investor protection since this will help the investor to protect their interests by assessing the risks they may incur in any decision the make in the securities market.

The market intermediaries must be qualified through obtaining of requisite license to deal in the securities. And their activities should be monitored and supervised by the authorized officials so as to ensure effective carrying out of their functions hence investors' protection.

And that in case of any complaint the investors should have an avenue to claim or raise complaints hence ensuring investors' protection. Here strict enforcement of the law is required in order for investors' interests may be safeguarded.

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<sup>67</sup>Objectives and Principles of Securities Regulation. International Securities Commissions, June 2010  
Retrieved on 4/06/2012 world wide web <http://www.iosco.org/about/>

### **3.3.3.2 Ensuring that Markets are Fair, Efficient and Transparent**

A fair market is where all parties in the market are treated equally and that not favouring other parties and leaving out others. Regulators through the set laws should detect and penalize those who manipulate the market or carry out unfair trading practices.

An effective market is the one that provide the relevant information to its investors in the required time frame and that the prices fully reflect all available information on a particular stock or market. Information has to be widely available in terms of accessibility and cost and released to investors at more or less the same time.

In a transparent market, communication between issuers and investors is open and easily accessible from either direction. The transparency should not only end with investors but must also be evident even to the public at large. It will enable a prospective investor access to the market and make comparison of the stocks before deciding to invest.

### **3.3.3.3 Reduction of Systemic Risks**

Regulation should aim at reducing the risk of failure in the market through capital and internal control. Where financial failure does occur, regulation should seek to reduce the impact of that failure, and in particular attempt to isolate the risk to the failing institution.

### **3.3.4 How the Market Operates**

The DSE is a central place where the exchange of shares or bonds takes place. It is a secondary market where existing shares and bonds, (i.e. securities already issued in the primary market) are being sold and bought. The existence of the DSE offers an opportunity for successful issue of shares to the public through Initial Public Offerings (IPOs) or when the company issues additional securities for the first time. Something to note, no company issues shares through the DSE directly. The shares are issued to the public in the first instance and thereafter traded at the DSE. Securities issued to the public for the significant

first time are done in a limited time of three to four weeks; trading beyond the permitted time is prohibited. The securities are sold to the public through selected receiving agents.

The secondary market is the exchange of the securities in the hands of investors amongst themselves. The securities are traded at the existing stock market value at the time. Commission shall be paid by the investor to the brokers on each transaction made.

### **3.3.5 Benefits of Issuing and Listing of Securities at the DSE.**

Companies that list at the DSE have more advantages than those that are not listed in the following aspects;

One, to obtain capital easily and cheaply from the public. This can be done through trading of securities which is done on a daily basis depending on the market of the said securities. This enables the companies listed to obtain capital which will facilitate the expansion and development of their entities.

Two, a good performance of a listed company since it is being monitored in the market so as to meet the expectations of the public. Once the company is listed the directors of the company are encouraged to meet the expectations of the investors hence adds to the credibility of the companies.

Three, listing of a company's securities provides for a venue for marketing the company since the company will be referred to on a daily basis in the stock market reports released to the public by the DSE. This is a marketing tool for these companies become household names.

Four, the ease in transferability of securities helps the company in obtaining funds from the public due to the existence of a ready market which will facilitate the sale of securities should the investors wish to the same.

Five, listed companies at the DSE are considered to be more efficient and reliable since they are subjected to scrutiny. Hence this makes listed companies superior to the unlisted ones.

Six, listing widens the range of financial choices of the company. This is because securities at the DSE are more flexible compared of those of unlisted companies.

Seven, it facilitates share ownership changes hence privatization since the public once obtain securities will also obtain a share in the company. Government owned shares can be sold to Tanzanians through the DSE as it was the case during Tanzania Breweries Ltd and other companies privatized through capital markets.

Eight, listed companies attract foreign portfolio investors. Listed companies are attractive to foreign investors as the investors knows the value of the companies to invest in and listing facilitates an exit mechanism.

Nine, the issuer will increase its opportunities to venture into investments and expansions by having alternative means of financing such investments. The flexibility created by listing the company on the stock exchange helps companies to expand into new ventures that would have otherwise not been possible due to lack of capital.

Lastly, listing adds to the status and public image of a company listed companies have a higher status than unlisted ones. This status has value in the sense that listed companies can borrow from banks at a cheaper rate due to marketability of their shares as well as being subject to other regulators over and above own regulations.

### **3.4 Fiscal Incentives**

The Government of the United Republic of Tanzania grants fiscal incentives to companies that are listed at the DSE so as to encourage more companies to be listed and hence encourage the development of the capital markets in the country. These incentives aim at facilitating the activities of the said companies and also facilitate in attaining

profits due to reduction of different taxes. The following are fiscal incentives granted by the government on companies listed at the stock exchange;

#### **1.4.1 Reduction of Corporate Tax**

Companies obtain a 30% to 25% corporate tax reduction for a period of three years under the condition that the companies' 35% of shares must be issued to the public. This incentive is applicable for companies that have been listed for five years from the date of first listing. The rationale of this incentive is to attract more companies to list at the Stock Exchange.

#### **1.4.2 Reduction of IPO costs in determining the income tax**

In making the Initial Public Offers (IPO), all costs incurred are considered by the TRA as expenses in generating of income from profits and hence are considered in determining the profit for tax purposes. This incentive is meant to make IPO costs tax deductible and extend the benefits to investors.

#### **1.4.3 Exemption of Stamp Duty tax on secondary market trades**

This incentive aims at enticing investors into trading in securities at the DSE. The exemption of the stamp duty reduces the cost to be incurred by the investors in selling and buying shares.

#### **1.4.4 Exemption of Capital Gains Tax**

Sale of listed securities shall not be subject to capital gains tax, whereas the sale of securities unlisted shall be taxed at a 10% tax rate. This incentive is there so as to encourage unlisted companies to list and trade at the DSE secondary market.

### **1.4.5 Reduction of Withholding tax on Dividend Income**

The withholding tax is charged from 10% for unlisted companies to 5% for listed companies at DSE. This incentive is aimed at encouraging more investors to participate on the DSE.

### **3.5 Listing requirements at the DSE.**

For a company to be listed at the DSE, it has to comply to specific conditions which will enable it to be in a standard fit to be offered to the public and have the required outcome. There are continuous conditions of being listed at the DSE of which a company must observe throughout its life as a listed company at the stock exchange<sup>68</sup>.

Firstly, for a company to be listed at the DSE it must first be a public company incorporated in the United Republic of Tanzania, with a minimum of seven shareholders. For a foreign company wishing to list, it must first be incorporated and obtain certificate of compliance before it can be cross listed.

Secondly, the company must have been operational for a period not less than three year and must each year have audited accounts. This will enable to establish the track record of the company, whether it is performing well or not.

Thirdly, it must issue at least 25% of its shares to the public. In this group not more than 1% shall be individual investors and 5% will be institutional investors. Shares owned by the employees are not considered to be part of the 25% ratio.

Fourthly, it must have at least TZS 500 million issued and paid up capital as of the year June, 2011.

Fifthly, it must be ready to comply with continuous listing requirements.

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<sup>68</sup> DSE Handbook, 2010 , pp 8-11

Lastly, the company should prepare a prospectus which must be submitted to the CMSA for approval, this is a document which will provide details of the company as to whether an investor to invest or not.

### **3.6 Continuous Listing Requirements at the Dar es Salaam Stock Exchange.**

Firstly, a listed company must inform the DSE on all dividends and cash bonuses recommended or declared together with the dates for closure of register and dates of payment of such dividends or cash bonuses. Also the decision to pass any payment of dividend or interest payment must also be made known to the exchange.

Secondly, the financial results for the financial year and the first six months of each financial year( interim report) such results are required to be announced within three months of the end of the end of the period concerned but are not to be audited the format and contents of such announcements are to be in accordance with guidelines issued by the exchange.

Thirdly, the DSE should be informed of any particulars of any new capital whether it is to be issued as capitalization or by way of right to shareholders.

Fourthly, the Exchange should also be informed of the changes in Directorate, the Secretary, Auditors and Legal Advisors and the date of the financial year end. This will facilitate the follow up on the activities of the listed companies and be able who is to be probed on questions on matters of management or audit.

Fifthly, any sell or purchase of assets which could alter the company's business or capital structure must be made aware to the DSE; this is so because every company to exist in the DSE listing it must possess a certain amount of capital and not below the set amount.

Sixthly, the listed companies must make known any other information that is necessary to enable the shareholders to appraise the position of the company and to avoid the establishment of false market in the listed securities. The said company must not release the information to a third party until it has been released in the market by the Exchange.

Lastly, the issuing company must forward as soon as it receives the copies of the Annual Report on Accounts, copies of half yearly interim statements and copies of all resolutions increasing the capital and all notices relating to further issues of capital or any other circular.

### **3.7 Key Market Players**

In order to be able to fulfill the listing requirements an issuing company has to consult professional advice at each step of the way until it is listed at the bourse of the DSE for trading. These professional are well trained in their fields hence ensure that the companies that list at the DSE comply with the standards and set requirements discussed above hence will ensure investors' interests are protected in the long run. These professional are;

#### **3.5.1. Lead Advisor**

Lead Advisor<sup>69</sup> is a firm which is appointed by issuers of securities as lead consultant in the IPO. The firm provide guidance through the whole process of making a company go public by coordinating all duties performed by other consultants for the company. The Lead Advisor makes the prospectus, carry out the valuation of issuers of securities, and submit the draft prospectus to sponsoring broker for on ward submission to the CMSA and DSE and further effect correction to the prospectus draft as per the direction of CMSA and DSE.

#### **3.5.2. Sponsoring broker**

Before a company can issue securities to the public, it must appoint a Sponsoring broker<sup>70</sup> who is a licensed dealing member of DSE. The broker acts as a link between the issuing company on one hand and the DSE and CMSA on the other hand. The

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<sup>69</sup> Issuers guide to Capital Markets; Capital Markets and Security Authority booklet, vol 1, p 21

<sup>70</sup> Ibid p 22

responsibility of the sponsoring broker is to make sure that the all the DSE listing requirements are complied with according to the CMSA<sup>71</sup> and DSE<sup>72</sup> regulations and rules.

Sponsoring brokers have functions in both the primary as well as the secondary market. In the primary market they sell securities on behalf of the issuers to the public; advising investors about issuances and providing investment advisory services to companies issuing shares.

In the secondary market which is the main focus of this work, the brokers act as agents by buying and selling their client's securities at a commission, advising the investors on matters relating to their investments or making further investments.

### **3.5.3 Dealers**

Dealers<sup>73</sup> perform the same functions as brokers but they have an added function that they trade in the secondary market as principals; this means they may buy and sell shares on their own behalf. They also referred to as market makers because they buy securities that they believe are under priced is right hence make profit from the difference in buying and selling prices.

In Tanzania all licensed brokers are dealers. When dealing as a principal, a dealer has to disclose the same to a client so that she /he can protect his/her interests.

A dealer is under the obligation to give priority to the needs of his client before those of his own. This can be guaranteed by timing the orders of the client upon arrival at the dealers office; hence protecting the interests of the investor.

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<sup>71</sup> Cap 79 R.E 2002 and its regulations

<sup>72</sup> Dar es Salaam Stock Exchange Blueprint

<sup>73</sup> Capital market intermediaries in Tanzania ;Capital Markets and Securities booklet, vol. 4, pg 4.

#### **3.5.4. Authorized Dealer's Representative (ADR)**

These are representatives of the dealers who execute transactions including placing orders and putting up business strategies at company level. In order for a firm to obtain license to operate as a broker/dealer is to have a part or full time basis licensed by CMSA as an ADR. One becomes an ADR after attending a three weeks course and must pass an exam administered by the DSE.

Another group are the floor traders who also place orders for securities at the DSE. They must also pass through induction course administered by the DSE.

#### **3.5.5. Investment Advisors**

For a company to obtain an Investment Advisor position<sup>74</sup>, it must fulfill all the requirements of a broker and dealer, it must be a bank licensed by the Bank of Tanzania (BoT); the main exception is there is no need of the CMSA course and exam. Investment advisors also have authorized representatives referred to as Authorized Investment Advisor's Representatives.

These key market players are people with qualifications and are under fiduciary duty to protect the interests of their clients. The DSE and CMSA also ensure that the same is protected by supervising every activity done by the professionals. Some of the groups such as the Licensed dealing Members (LDM) must undergo special training in order to be able to work in the market. The training is on matters such as market practices, finance, the securities regulations, preparation of memorandums and prospectuses.

#### **3.5.6 Receiving Bank and Collecting Agents**

Issuers normally do not have the infrastructure and resources to handle high volumes of applications and cash from the public. Thus, regulations require issuers to appoint a bank to act as a Main Receiving Bank. This bank has the overall responsibility of ensuring that

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<sup>74</sup> Capital market intermediaries in Tanzania ;Capital Markets and Securities, vol. 4, pg 5.

all monies and forms collected by all receiving agents reach the bank according to the contracts ( Sales Level Agreement). The main bank coordinates all other receiving agents that may include banks, brokers, dealers, Tanzania Post Corporation or any other organization appointed by the issuers for that purpose.

### **3.5.7 Reporting Accountant**

Is an accountant required to assist the issuer by looking at the way accounting data has been compiled in the issuance document, including assumptions and forecasts. The reporting accountant provides an independent evaluation of the company's financial reports. In order to ensure independence, the role of reporting accountant cannot be performed by the company auditor. The segregation is in accordance with the National Board of Accountants and Auditors (NBAA)<sup>75</sup> specifications..

### **3.5.8 Legal Advisors**

These are responsible to guide the issuer according to the CMSA Act. They draft contracts with other service providers on behalf of the issuer, give legal opinion on the legal existence of the issuer, its ownership of assets and properties as well as reviewing any pending litigations of the company.

## **3.6 Conclusion**

These two bodies the CMSA and DSE enable the proper function of the securities business in the country by providing the necessary environment for the growth of the market and confidence of the investors in the market and the listed companies at the DSE. There are a set of guidelines and rules which enable the market to function while safeguarding the interests of both the listed companies and the investors themselves. Through the use of market intermediaries the companies wishing to list at the

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<sup>75</sup> The role of NBAA is relevant to preparation of financial statements and disclosure standards which are significant in the regulation of capital markets in relation to investor protection and transparency at the market.

## CHAPTER FOUR

### FINDINGS AND DATA ANALYSIS

#### 4.1 Introduction

The data analysed in this chapter was collected from the offices of the DSE's and CMSA's the legal departments, the stock brokers and the licensed dealing members (LDMs) and the individual investors from the listed companies at the DSE. The aim was to determine whether there is protection of individual investors at the market, with emphasis on the law relating to the stock market in the country.

#### 4.2 The stock brokers and the LDMs

The researcher had the following findings from a visit at six of the seven securities brokerage firms in the country. The findings are as per the set of questions that were used during the interviews.

##### 4.2.1 Interaction with Clients.

All the stock brokerage firms upon receiving a client for the first time made them aware of what stocks are and the benefits investing in them which are; obtaining dividends periodically from the profits of the companies they have invested in; obtain benefit through capital gains through appreciation of the investment in time if the investment is a good one; and stocks can be used as a security for people who wish to take loans from banks.

Moreover, investors are to be informed of their rights and duties as investors of the said companies listed at the DSE. The said rights are listed under Section 133(1)<sup>76</sup>, which states that;

*Every company shall in each year hold a general meeting as its Annual General meeting, and shall specify the meeting as such in the notices calling it. At the Annual General Meeting... transact the following business;*

- (a) To have laid before the members the annual accounts;*
- (b) To have laid before the members the directors' report;*
- (c) To have laid before the members the auditors' report;*
- (d) The appointment of auditors for the period of the next general meeting at which accounts are laid;*
- (e) The re-election of directors retiring and seeking re-election...*

About 75% of the firms stated that they did inform their clients of their rights such as attendance of Annual General Meetings (AGM) where they can take part in decision making of the companies through voting; obtaining periodic dividends from profits of the company, inform the clients on how to obtain financial information of the company either through the AGM, the media, the brokers or at DSE or CMSA.

The dealers and brokers may inform the client of their rights as investors depending on the knowledge the investor has about the securities market on his/her rights. This assumption does not give each investor the opportunity to learn in detail what is expected of him/her as an investor. Therefore the said investor will not make a proper follow up on the progress of the company he/she has invested in and in case of any problems such non-payment of dividends or poor performance of the company the investor's confidence in the market is lowered.

It is then the duty of every dealer and securities brokers duty to make sure that every investor is made fully aware of his/her role in the market in order to be able to make informed decisions in relation to his/her investment, for example when to decide to sell the stock depending on the performance of the company so as to make profit from the

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<sup>76</sup> Companies Act, 2002

sold stock and when to buy more stock from a said company due to its good performance in the market..

#### **4.2 2 Regulation by DSE**

The brokers and LDM stated that the DSE made sure that they follow the regulations of the stock exchange such a making sure that each client who deposits money with broker is kept in a Trust Account made for such client immediately upon obtaining the funds; this is so as to avoid misuse of clients money. The time limit for staying with client's money who wishes to buy stock depends with the agreement between the broker and the client since stocks at times are not readily available, if no transaction is done the money should be returned to the client at the agreed time or else he may file a complaint, this is according to practice. The law under section 69(1) provides that;

*...(1) A dealer shall open and maintain with a bank in Tanzania an account designated as a trust account.*

*(2) A dealer shall pay into such account all moneys held by him or a client not later than the next day on which the bank is in business following the day in which the moneys are received by the dealer.<sup>77</sup>*

Therefore, upon reception of a client's money, the dealer has up until the next working day to have opened a Trust Account for the client with the Bank of Tanzania (BoT) any other bank in Tanzania as provided for under Rule 3.54 (a)

*...Each LDM shall establish and keep in a bank or banks in Tanzania one or more Trust Account, designated or evidenced as such, into which it shall pay;*

*(a) All amounts(less any commission and other proper charges) that are received from or on account of any person (other than an LDM) for the purchase of securities;..<sup>78</sup>*

The DSE and the CMSA monitor the clients accounts so as to make sure things are in order. The said funds in the Trust Accounts shall be used as per the instructions of the client in purchase of securities.

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<sup>77</sup> Cap 79 R.E 2002

<sup>78</sup> DSE Blueprint

And the DSE shall supervise the transactions in such accounts as provided for under Rule 3.54(c)

*....c) (i) The Trust Account shall be designated client's account and shall solely receive moneys deposited by clients for the purchase of securities and effect payments for securities;*

*(ii) The Trust Account shall not under any circumstances be co-mingled with any other bank accounts operated by the LDM; and*

*(iii) The Exchange shall have power to inspect the operations and activities of all Trust Accounts maintained by the LDM at such intervals as may be determined by the Council.<sup>79</sup>*

It is an offence for a broker to misuse a client's money<sup>80</sup> may be fined an amount of two million shillings or imprisoned. Exim Securities<sup>81</sup> was banned for the misuse of clients' money in the year 2000, while Core Securities was suspended for a year in 2009 for price manipulation of the TBL shares<sup>82</sup>.

The brokers also highlighted practices which the DSE prohibit them to do which would defraud an investor. Prohibited practices such as insider dealing, price manipulation, false trading and market rigging. In deciding the fate of the broker the CMSA is also involved since is the main supervisory body of the stock market in the country. A broker if found guilty may either be warned or suspended for a specific duration or lose their license<sup>83</sup> depending on the severity of the offence the DSE Council shall apply its discretion.

Insider dealing is considered as a practice which is difficult to prove despite the supervision done by the DSE and CMSA. A broker was suspended for a year by the CMSA for advertising of securities before the set time by the CMSA.

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<sup>79</sup> *ibid*

<sup>80</sup> Section 70 of Cap 79 R.E 2002

<sup>81</sup> Exim Securities is one of the earliest securities brokerage firms which started trading at the DSE immediately after DSE establishment.

<sup>82</sup> Interview conducted with Mr. Gabriel Malauri a Licensed Dealing Member from Orbit Securities in Dar es Salaam.

<sup>83</sup> Rule 3.22 of the DSE Blueprint

### **4.3 Individual investors**

The questionnaires were submitted to eighty (80) individual investors at different locations in Dar es Salaam at their work places. The majority of individual investors who filled the forms were 75% males and 25% females. In this group all the candidates were educated people with different professions from lawyers, teachers, accountants, economists, businessmen and women.

Further the rate of risk taking in making investments by comparing different age groups differ by being higher in the age between 50-70 as compared to that of 35- 50. The older group has more shares and more diversified by buying shares from different companies at large amounts. This signify that they take a higher risk because they are well informed of their rights as investors compared to the other groups and understand how the market works, hence reduces the fear of loss.

The group between the age of 18-35 is an upcoming group as investors since they have less number of shares due to low risk taking, this is due to not knowing how he market operates and fear that their investments will be lost and the need for quick profits from investments. This means that they are low awareness on their rights and in case of default or grievances the right channels to per sue.

Most individual investors have invested in Tanzania Breweries Ltd (TBL), Cooperative Rural Development Bank (CRDB), National Micro- finance Bank (NMB), Tanzania Cigarette Company (TCC) and TWIGA with shares ranging from 1000-2400. This is due to the good performance of the companies in the market where there is adequate disclosure on the financial standing of the companies in the market hence brings about confidence in investing in the said companies; this signified by the fact that these companies are more transparent by holding Annual General Meetings at regular intervals hence keep the investors up to date on the happenings of their investments. While in the other companies individual investors invest less due to poor disclosure of the financial

position of the companies as in Tanzania Oxygen Limited (TOL)<sup>84</sup>, Tanzania Tea Packers (TATEPA). Some investors complain that the companies they have invested in do not provide dividends and do not have any information on the going on of the company which will put the investor in a comfortable position to make decisions relating to their interests in the companies.

Moreover more than 90% of the investors have awareness of their basic rights as investor where the remaining 10% have no awareness. Some of the rights that the investors are aware are the voting rights, attendance of Annual General Meetings hence getting involved in the decision making of the companies he has invested in.

#### **4.3.1 Complaints made by investors.**

Up to 80% of the investors did not have any complaints raised in the services provided by the licensed dealing members and the brokers. This means that they were satisfied with the work done by the DSE and CMSA in supervising the LDM and brokers in handling the interests of their investments in the market.

The other 20% had complaints to the brokers and the companies they had invested in. They stated that the brokers did not execute their order on time either on buying or selling of shares. Other complained that the companies they have invested in do not provide any information since dividends are no longer paid, a good example is the TOL<sup>85</sup> and this has

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<sup>84</sup> TOL is one of the first companies to be listed at the DSE upon its establishment. The initial price for company shares was Tshs. 500 and briefly went up to the maximum of Tshs. 520 before it dropped to Tshs. 190 in May 2004. The annual accounts for the period ended in December, 1999 revealed that the company had made a loss of 1.76 billion shillings, hence no dividends to shareholders. Currently due to restructuring of the companies management and production its share price has risen from Tshs. 190 to Tshs. 220 in year 2011/2012

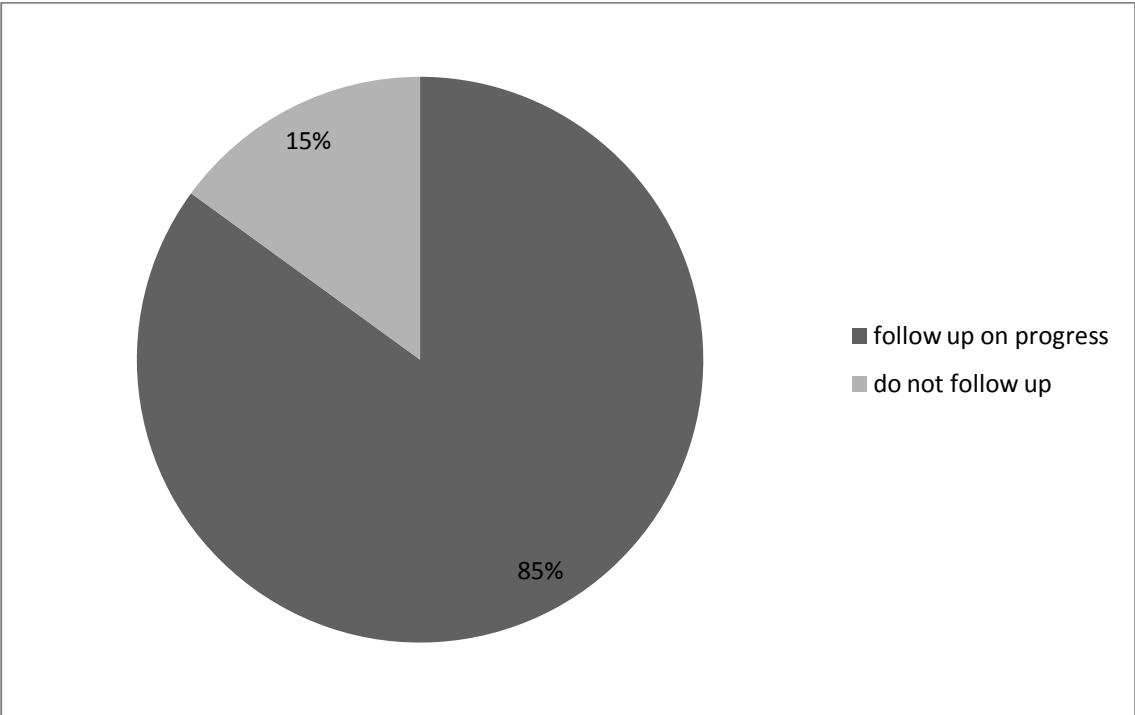
<sup>85</sup> The company had not been performing well due to the poor management of the directors; investors who later invested in it were those who believed that the company's profits will change with time due to improvement of the management and hence a more efficient production by Marwa. M; Equity Research, TOL gases Ltd Local Listed Company; Tanzania Securities, pg 1

been going on for years and the market regulators such as the DSE and the CMSA have taken too long to take action hence the investors interests continue to be jeopardized.

When this group which raised complains were asked as to the measures taken to settle their grievances, those with issues on buying of shares were compensated their money by the brokers and as for those that had claims against the companies, no measures were taken to inform the investors on what was happening in the management of the company.

The investor is seen to be able to file a complaint with the CMSA for the change of management of companies that have directors who abuse their office instead of working for the benefit of the investors. As for the case of NICOL, its investors have the right to sue the management for their investments since they had not complied with the listing requirements which lead them to be delisted from the exchange.

**4.3.2 Progress of the company.**



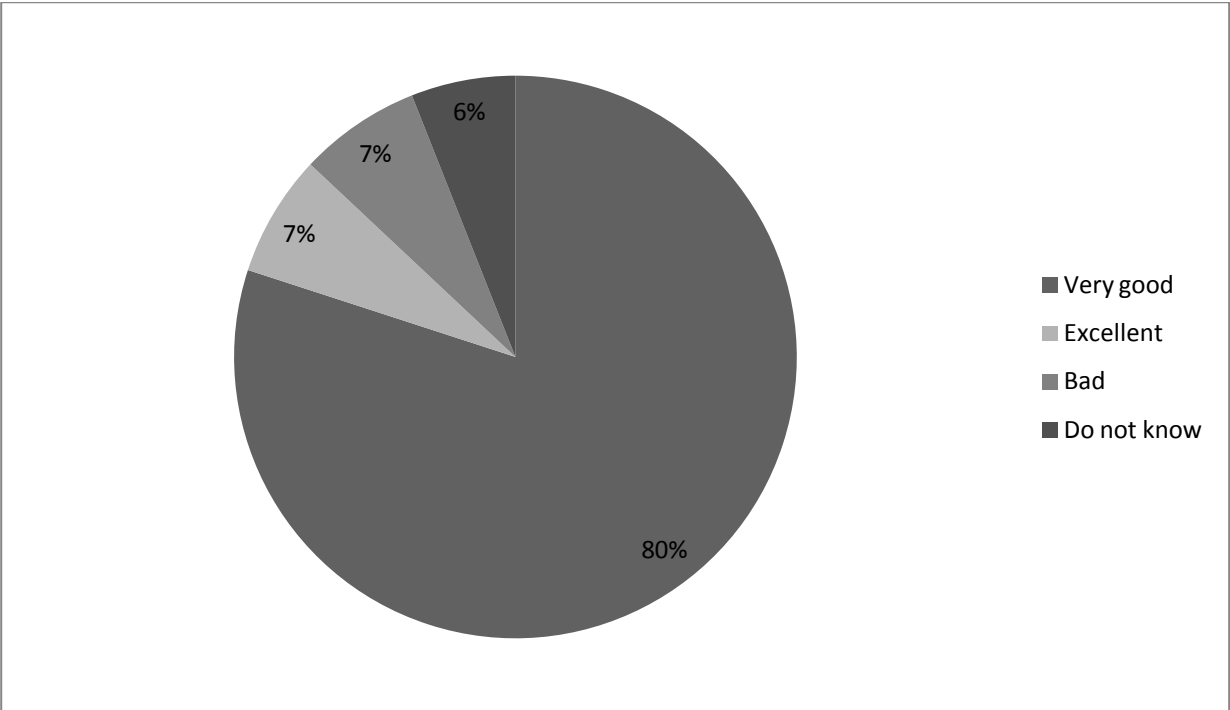
**Figure 1: Data obtained on Investors' follow up on progress of their invested companies at DSE**

Around 85% of individual investors made follow ups on the progress of the companies they h have invested in. this was done through attendance of AGM, through the news media which is through reading news papers, listening to the radio and watching television; some obtained information on their companies through the brokers or by visiting the company itself or the DSE.

The remaining 15% do not follow up on the progress of the companies they have invested in even though there are methods made aware to them of knowing how the company is performing in the stock market.

Following up on the progress of a company can help an investor know things like increase or decrease of dividends due to profit or loss of the company, or where there is a case of no dividends due to use of profits to expand the business. This will help the investor be aware and realize whether his interests are being safe guarded or not.

**4.3.3 Disclosure of information.**



**Figure 2: Data obtained on Level of disclosure of information at DSE listed companies**

Nearly 80% of individual investors consider the disclosure of information to be very good. This means whenever required it can be obtained from the licensed dealing members or brokers, through the media, at the Annual General meetings or from the DSE and CMSA. Another group of 7% considers the flow of information in the stock exchange dealings to be excellent. And 7% consider the information flow to be very bad, that is they find it difficult to read the financial statements provided by the companies through the brokers, the media and the DSE. They lack the knowhow of reading the balance sheets and statements in order to determine the progress of the companies they have invested in. and the remaining 6% did not have any comment on the issue of disclosure of information by companies listed at the stock exchange.

#### **4.4 DSE and CMSA management**

Interviews conducted in the legal departments of both DSE and CMSA on how investor protection was guaranteed as the regulatory bodies of the stock market in the country.

##### **4.4.1 Investor Education on their rights and duties in the market**

This education usually aims at giving the general public awareness on investment in stocks. The awareness creation is provided through news media such as television, radio, news papers, brochures and pamphlets, crowd pulling event such a “Saba Saba” and “Nane Nane” Shows; seminars conducted all over the country at district level.

Such awareness creation is centred on informing individual investors of their rights as investors such as obtaining dividends, attendance of AGM, and their rights as shareholders such as voting rights so as to take part in the making of decisions in the companies he has invested in. The Authorities are also centred on making people aware of the disadvantages of being involved in pyramid schemes scams which will cause them to lose their money. They also educate on who are genuine brokers so as to avoid fraud of investors’ money from people who are not qualified to trade in the market.

##### **4.4.2 Control of market intermediaries**

The main focus of the market intermediaries were the brokers and the licensed dealing members (LDM). Regulation of their activities begins from the moment one obtains the license; this is through deliberation of the Council of DSE to admit an application of an LDM, who must also pass through an exam se by the CMSA with a pass mark of 75% in order to obtain a practicing certificate. A broker and LDM must a have a running capital of 10 million and 20 million respectively.

The transaction carried out by the brokers and LDM are monitored through the CDS accounts of the clients or through on-site inspection at the brokerage firms. The accounting records are checked for order, the staff at the brokerage firms are observed for competence, if there was a request from the CMSA for any competence report on any

trading transaction, the firm must provide. Further that the trading rules are fully complied with when trading for a client.

Prohibited practices will be traced through monitoring of the clients account and through on-site inspection conducted by the officials from CMSA. A good example is in the year 2000 the brokerage firm that was banned from operating for misuse of clients funds<sup>86</sup>. Another securities brokerage firm was suspended for the prohibited practice of price manipulation of TBL shares in the year 2009.<sup>87</sup>

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<sup>86</sup> Exim Advisory Securities was one of the earliest brokerage firms in the country.

<sup>87</sup> Core Securities which is still operation to date.

## **CHAPTER FIVE**

### **SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS.**

#### **5.1 Summary of Findings**

The Dar es Salaam Stock Exchange is the only stock market in Tanzania, where trading of stocks and bonds is carried out. Through the brokers and the licensed dealing members, shares and bonds of the investors change hands through buying and selling at the market. It is called the secondary market because shares which were sold at the IPO are now sold at this market, here the investors change hands on the shares they own.

The DSE regulations and Blueprint provide the guidelines under which the said trading should take place so as to ensure the interests of the investors are safe guarded and that the activities of the stock market run smoothly. The CMSA is the supervising body of the DSE; it oversees the activities done by the stock market ensuring that rules are followed by the licensed dealing members, the brokers, the investors and the said companies listed at the DSE.

The DSE and the CMSA ensure that investor protection is safeguarded by ensuring that the listed companies provide interim and annual financial reports on the progress of their companies hence making investors aware of their investments' position; default of which will lead to warnings and finally delisting of the said company. Again, the DSE and CMSA oversee the conduct of the brokers and licensed dealing members, to ensure objectivity in the securities business. That the individual investor is informed of his rights and responsibility to his investing company. And that the brokers observe the law in their day to day activities in the market.

However, the CMS Act clearly stipulation of the prohibited practices in the market such as insider dealing with all essentials to make it an offences but there is lack of adequate technology which limits the detection and collection of proof on offenders.

Listed companies provide annual financial statements of which not many investors have the ability to read and understand; hence make it difficult for investor to grasp the financial position of their companies so as to decide whether to sell or buy more shares. New investors will be intimidated with financial statements due to lack of interpretation skills, hence lowering of the confidence in the market. And at times letting a broker help to interpret the same requires time, to visit their offices of securities broker, of which not many investors have. Again the location of their offices is also a hindering factor, this because majority of offices are located in Dar es Salaam. This limits the investors from out of town to get access to such assistance.

Further, not many individual investors are fully aware of their rights as investors; majority are only aware of the aspect of obtaining dividends and that they may take part in voting in shareholders meetings of the companies. This limits the participation of the individual investors in the market due to lack of enough awareness. This makes it hard for the investor to identify prohibited practices in the market due to ignorance of the same. Knowing the fraudulent practices will empower the investor to follow the law to get justice since one will know when his/her rights have been infringed.

Moreover, some individual investors for fear of procedure tend to ignore their investments which do not produce dividends hence letting go of their rights. This is so because the said procedure is not clear as where to address their problems either to the companies concerned or to the DSE or the CMSA. Or at times the procedure is clear to some individual investors but they take investments generally as taking risks even when their rights have been infringed therefore do not make follow up. There is a need of making it clear what kind of risk is legally allowed and which is not so as to allow effective protection of investors.

Further, the law has clearly defined prohibited practices in the stock market, but how an investor can be able to trace and identify that injustice is being done to his investment is still unclear. There should be a proper education on how one can be able to learn the same by having access to his CDS account to check transactions.

The law clearly sets out the prohibited practices at the stock market but it is evident that from the technology available it is difficult to carry out proper supervision in the market as in the case of insider dealing. A higher technology is need to collect the evidence needed to prosecute offenders of insider dealing; since a person proof of guilt must be beyond reasonable doubt. Therefore without tangible proof those suspected of insider dealing may walk free. Moreover, as per securities law a dealer is not to give priority to his orders when he has the same from a client. The control mechanism is timing the orders of the client upon entering the offices of the dealer; this is very unrealistic approach since the dealer may decide to record differently and it will not be possible to trace the same. And again not every client wishes to buy or sell shares upon visiting the broker's office.

Moreover there has been poor publication of the disciplinary actions taken against the brokers and LDMs. Making public of such actions by the DSE and CMSA will enable the investor to be more informed hence make a close follow up when it comes to his/her investment in the stock exchange. As much as publicizing is not advantages for the growing market but will entail more transparency hence increase confidence of the investors in the stock market.

Generally, there is protection of investors despite the few setbacks; which once improvement is done the market will flourish with more investors. This is by increasing awareness in the current investors at the listed companies of the DSE who in turn will be better advocates of the stock market industry to fellow Tanzanians and foreigners hence encouraging more investments. Protection of investors will be better guaranteed once the individual investor himself is knowledgeable on the laws and procedures in the market hence enables him to follow up on his/her interests; where there is infringement of the law the investor will know where to go and procedure to follow.

## **5.2 Conclusion**

The DSE under the supervision of the CMSA has managed to regulate the developing stock market in the country; by the application of strict rules and regulations through regular follow ups of the activities of the stock market specifically of the companies listed at the stock exchange, the stock brokerage firms and other investment advisors. This is so as to ensure an orderly, transparent and efficient market which will encourage more investors to take part in.

However there are a few setbacks that make the market not to grow as rapidly and as effective, the main one being low awareness of individual investors in the operation of the stock exchange. This starts from the beginning where an investors is to read a prospectus and decide whether he wants to invest in the said company, to the quarterly and annual financial statements of the company to be invest in. The individual investor is seen to lack the adequate skill to process the information and hence depend on the word of the stock broker instead of his own intellect, which at times could benefit the interest of the broker and not the client/ investor.

Moreover, an individual investors is challenged on the matter of taking legal action against a stock broker or a company for misappropriation of funds, because there are no clear channels that are set out to be followed which are disclosed from the moment one enters the market to trade, so that one can protect, his or her interest and where litigation is concerned it is considered too costly. This makes individual investor fear investing in the stock market.

Further, the said prohibited practices are well outlined in the law but their detection is still a challenge in order to prove and convict the said persons involved. Unfortunately when broker of LDM has been taken for disciplinary action, it is publicized enough so that the investors are made aware. This will enable to learn more about the prohibited practices and know which stock broker is suspended or banned from practicing hence facilitate effective application of the law.

### **5.3 Recommendations**

For protection of investors to be further guaranteed in the stock market there is a need to increase awareness in the current investors in the market of their rights and responsibilities in the market. This is because a client well served will be better than any advertisement for the stock market industry. Here investors themselves will educate other people on the benefits of investing in the market. This will contribute to the effort made by the DSE and CMSA to increase number of investors in the stock exchange; at the same time guaranteeing investor protection, this so because now the investor will have more understanding of the market which will facilitate protection of his interests. Education should be centred on how to read the financial statements of the listed companies and understand them so that they may be able to observe the progress of their investing companies at the DSE.

Secondly, provide other means of understanding the financial position of the listed companies apart from the financial reports of which majority individual investors are not able to read and understand. Interpretation of the said financial statements may be made in words so that investors who wish to be informed may understand the operations of their investing companies without any inconveniences. This will serve the as means of protecting the investors interests hence enable the effective application of the securities law in the country.

Thirdly, there is a need for improvement of technology so as to increase the chances of detecting the prohibited practices such as insider trading. This is because currently it has been difficult to prove any allegations relating to insider trading due to lack of means to trace the flow of the confidential information from the insiders to outsiders hence difficulty in apprehending offenders due to lack of tangible proof. An improved technology will enable the law on insider dealing to be effectively applied hence protecting the investor in the process and the listed company concerned.

Fourthly, the courts should be more accessible to individual investors' claims through lowering of costs of the commercial cases. A good example is the NICOL situation where

by individual investors are to sue the company for their investments because of failure of obtaining any dividends and lack of timely financial information on the company's activities which considered to be infringement of their rights but the cost of instituting such as case is a major hindering factor for individual investor therefore limits the application of the law , which enables the investor to obtain justice from the loss suffered due to the default of the listed company at the DSE. Therefore the DSE and the CMSA should assist the individual investors who wish to sue to facilitate the suit by providing the necessary evidence where needed and also providing guidance to the investor who was assured protection upon entering the stock market by the DSE and the CMSA. This would increase confidence of the individual investors greatly since they will be sure that even when there is default their interests will also be safeguarded by the two bodies that control the market.

Fifthly, delisting a company by the DSE which has failed to meet the requirement does not fully protect the current investors since the defaults are done by the listed company since the investor is left out to follow up on recovery of their investments at their own costs. There is a need to look on improved regulations and law that not only protect a prospective investor but also a current one who finds himself incurring loss from the acts of the management of the listed .therefore when the company is consider for delisting there should be well laid out plans that will protect the interests of the investors.

Sixthly, the CMSA and DSE should encourage the LDMs and brokers to provide more information to every new investor upon entering the market from the benefits of investing to the remedies available upon default and the bodies concerned. This will help the new investor to be aware of the operation of the market and ways of being compensated in cases of loss caused by fraudulent acts of the brokers or the LDMs or the management of the listed companies themselves and in what circumstances.

Seventhly, the DSE should encourage the LDMs and brokerage firms to open up offices in other cities in the country so as to be able to reach the investors who are far away from Dar es Salaam. This is because the brokers and dealers will assist the investors in

understanding the position in the companies they have invested and in case of questions they may obtain access to the dealers and brokers easily compared to how things are now.

Lastly, the regulatory authority such as DSE and CMSA upon instituting disciplinary action against its members such as LDMs and brokers there should be publicity of the same in the news media; this will help the investors to know the status of the professionals on whom they depend on for investment advice. This will provide awareness to the individual investors of the related capital markets offences hence be able to report the same in situations that they may encounter the such offences. Currently disciplinary action is taken but the mass are not aware of, this makes the market to less transparent.



If the answer is yes, what are those right that u are aware of

.....  
.....

6. Have you ever made any complaints due to unsatisfactory services given by a broker?

Yes  No

If the answer is yes, please explain the cause

.....

7. if the answer is yes from above question, what measures were taken

.....  
.....

8. Are you aware of the laws that deal with the stock market in the country?

Yes  No

If the answer is yes, mention them .....

.....

9. Do you follow up on the progress of the company you have invested in?

Yes  No

If yes, how?

.....

10. How do you rate the disclosure of financial statements of the listed companies at the DSE?

Bad  Good  Very Good  Excellent  I don't know

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