



**MYERS, FLETCHER & GORDON**

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# NEWSLETTER

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## THE JUNIOR MARKET - A STIMULUS FOR YOUR BUSINESS



**T**he Ministry of Finance and Public Service and the Jamaica Stock Exchange are well advanced in their efforts to launch a Junior Market in Jamaica. The aim behind the creation of this Junior Market is to enable small and medium sized enterprises to raise capital from the public.

The proposed rules for the operation of the Junior Market are presently in the draft stage and can be downloaded free of cost from the Jamaica Stock Exchange website.

The criteria for listing on the Junior Market contemplated under the draft rules include:

- a) an intention to raise no less than \$50 million and no more than \$500 million;
- b) that the entity is neither wholly or partially a subsidiary of a registered entity on a recognized stock exchange;
- c) that the entity itself is not listed on the main board of the Jamaica Stock Exchange;
- d) payment of a listing fee (expected to be up to 50% lower than comparable fees on the main board of the Jamaica Stock Exchange); and
- e) an agreement with a mentor, acceptable to the JSE Board, who will provide guidance regarding compliance issues such as good standards of corporate governance.

The draft rules contemplate a number of benefits for persons listed on the Junior Market; these include:

- a) a full income tax holiday for the first 5 years after listing;
- b) a half income tax holiday for the second 5 years after listing;
- c) an exemption from tax on dividends or other distributions; and

- d) an exemption from transfer tax and stamp duty on transfers of shares in companies listed on the Junior Market.

It is expected that a company listed on the Junior Market will graduate to the main exchange within ten years and will remain on the combined exchanges for at least 15 years. If the company delists within 15 years it will be required to repay to the government the tax benefits enjoyed during the period of listing. Although it has not been expressly stated in the draft rules, it is presumed that this requirement for repayment of tax will apply only to income tax benefits received since any relief on transfer tax, stamp duties, dividends or other distributions will enure to the benefit of the investor and not the company itself.

An entity is not required to list all its equity on the Junior Market and may limit its listing to not less than 20% of the participating voting share capital. However, this 20% must be held by no less than 25 shareholders in the first 5 years and no less than 50 shareholders during the next 5 years. The existing principals of the company may therefore retain control of the company while taking advantage of the benefits noted above.

The JSE plans to considerably simplify the process for listing on the Junior Market, through the use of standard form documents, and publication of the approved prospectus by electronic submission to the JSE which will be uploaded to the JSE's website.

If listing on this Junior Market is something that you may be interested in, please do not hesitate to contact us. We would be happy to:

- (i) discuss the benefits of listing on the Junior Market;
- (ii) advise on the requirements and ongoing obligations;
- (iii) customize, where appropriate, the JSE standard form documents; and
- (iv) assist with the process of listing.

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## COMMERCIAL USE OF A PERSON'S IMAGE



It is common for local companies to use the image of a non-celebrity to promote its product or service. The usual approach of these entities is to either contract with an individual directly or to employ the services of marketing companies to do the contracting.

It is important that corporate entities seeking to use an individual's image to promote its product or service appreciate the need to obtain the consent of that individual (preferably in writing). The agreement should not only provide for use of the image but also include a full understanding as to the nature and scope of use.

All agreements should have clear, unambiguous provisions that address the following:

1. Appropriate provisions identifying the owner and controller of the image or personality under consideration. One must ensure that the person with whom he/she is contracting with warrants that he/she has the right to license the use of the image.
2. Identification of the image and the indicia that is being licensed.
3. The scope of the use of the image must be clear; and the following questions answered:

- a) Is the image to be used in any medium whatsoever?
- b) Is the image to be used to endorse all or only some of the company's products?
- c) Is the image to be used for a set period of time or is it indefinite?
- d) Is the image to be used exclusively or will the image rights holder be entering into other contracts with other entities?

4. Appropriate compensation for the use of the image by way of a royalty or a flat licence fee.
5. Whether there is a right of first refusal in the contract. This ensures that when the contract is coming to an end, the image rights holder is obligated to enquire as to whether the other party wishes to renew the contract before contracting with another entity.

For further information and advice regarding image rights, please feel free to contact the writer.

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## BANKING REGULATIONS DESIGNED TO PREVENT FAILURE OF THE BANKING SECTOR - POST FINSAC



During the 1970's to the early 1980's, the legal regulatory framework permitted formation of merchant banks and building societies with much ease. The firewall between banking, insurance, money management and other financial services was eroded, giving rise to "groups" of companies. These groups often comprised an insurance company, commercial bank, merchant bank, building society and perhaps a mutual fund or unit trust.

The state of affairs encouraged laxity in decision making, reliance on too highly leveraged operations and too many intra-group loan accommodations. By mid 1996 the indigenous financial services sector collapsed. The following features were common among the failed financial institutions:

- failure to comply with proper internal control procedures;

- poor risk management and inadequate portfolio diversification;
- poor quality of management and strategic planning;
- failure to exercise due diligence and care;
- unusually high risk appetite;
- a high incidence of connected party lending; and
- breach of directors' fiduciary duties and fraud.

In 1997 the Financial Services Adjustment Company Limited (FINSAC) was formed by the government to intervene, rehabilitate and dispose of elements of the financial services sector that would, in the normal course of operations, be unprofitable. Additionally, amendments were made to existing pieces of legislation and, in some instances, entirely new pieces of legislation were introduced. The objective of the new regulatory framework was to improve the soundness and reliability of the Jamaican financial system by increasing levels of probity, market discipline and better risk management.



## The Legal Framework in the Post FINSAC Era

Commercial banks, merchant banks, investment companies and firms, building societies and credit unions are supervised by the Bank of Jamaica and Financial Services Commission. The legal regulatory framework for banks and other financial institutions includes: *The Banking Act* for the regulation of commercial banks; *The Financial Institutions Act* for the regulation of merchant banks and other licensees under the Act; *The Building Societies Act* for the regulation of building societies; *The Securities Act* for the regulation of securities dealers, investment advisers and other licensees under the Act; and *The Co-operative Societies Act* for the regulation of credit unions.

The Bank of Jamaica also supervises the following money service businesses: cambios, bureau de change and remittance companies. *The Proceeds of Crime Act* introduced more stringent requirements in relation to effective monitoring and prosecution of money laundering through the financial sector.

The legislative framework designed to promote an effective and reliable financial sector includes several mandatory requirements that affect the operations of banks and other financial institutions. Under the *Financial Institutions Act*, merchant banks and other licensees are required to adhere to the following standards:

1. Capital Base: At least \$25 million
2. Maximum Deposit Liabilities: 20 x Capital Base
3. Limits on Lending Operations such as:
  - unsecured lending to connected persons except employees is not allowed;
  - unsecured credit to an employee must not exceed 1 year's emoluments;
  - unsecured credit to any individual or entity must not exceed 5% of Capital Base;
  - unsecured credit to a connected group of companies must not exceed 10% of Capital Base;
  - secured credit to any individual or entity must not exceed 20% of Capital base; and
  - secured credit in aggregate to any group of companies must not exceed 40% of Capital Base.
4. Capital to assets ratio:
  - Capital Base to Total Assets-Benchmark 6%;
  - Fixed Assets at Historical Cost to Capital Base-Maximum 1:1, i.e. not exceeding 100%.

5. Cash Reserve: At least 5% x Prescribed Liabilities.

*The Banking Act* requires that commercial banks adhere to the following:

1. Capital Base: At least \$80 million for local banks and at least \$250 million for foreign banks.
2. Maximum Deposit Liabilities: 25 x Capital Base.
3. Limits on Lending Operations for:
  - unsecured credit to connected persons;
  - unsecured credit to an employee;
  - unsecured credit to any firm or corporation which holds 20% or more of bank's capital;
  - unsecured credit to any firm or corporation in which the bank or a connected person has an interest as a partner;
  - unsecured credit to a shareholder holding or controlling 20% or more of the voting shares;
  - unsecured credit to any person who holds or controls 20% or more of the bank's shares; and
  - unsecured credit to any firm or corporation if the credit facilities are guaranteed by a connected person who in relation to that firm or corporation has an interest as a partner, or holds or controls 20% or more of the voting shares.
4. Cash Reserve: At least 5% x Prescribed Liabilities

## Recent Supervisory Developments-Basel II

In June 2004, the Basel Committee of Banking Supervisors issued the New Capital Accord commonly referred to as Basel II. This is a revised framework for the computation of capital adequacy for internationally active banks and was being promoted for adoption by all G-10 member countries by 2007. The primary objective of this new Accord is to introduce a more risk sensitive capital requirement and by so doing, promote stronger risk management practices within the banking industry.

The Bank of Jamaica will be adopting Basel II under a four phased approach ending in full implementation by 2010.

## Conclusion

The introduction of stringent regulatory monitoring and controls by the respective agencies subsequent to the financial markets meltdown in the 1990's provide the appropriate guidance and framework under which sound banking practices are enforced.

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# ISSUING SECURITIES TO THE PUBLIC - EXEMPTIONS FROM REGISTRATION OF A PROSPECTUS



In June 2008 the Financial Services Commission's ("FSC") Guidelines for Exempt Distributions ("the Guidelines") came into force. These Guidelines relax the requirements for the issue of securities in Jamaica, in that, a prospectus need not be registered with the FSC before a public

offering, where certain conditions are met.

The Guidelines establish circumstances in which an issue of securities will be treated as an exempt distribution in which registration of a prospectus is not required. Broadly described, these circumstances are:

1. where the issuer makes an issue of securities to a person whom he/she reasonably believes is an accredited investor. Accredited investors include banks, insurance companies, financial institutions, building societies, an individual whose net worth exceeds \$50 million dollars, or corporations in which such a person holds over 90% of the voting shares;
2. where the issue of securities is to a person purchasing as principal securities with an acquisition cost of not less than \$10 million paid for in cash and the trade is in the security of a single issuer;
3. where highly rated debt securities are being issued to a person as principal. Highly rated debt securities are securities that meet the following criteria:
  - (a) the security has a been rated as BBB+ by a recognized rating agency;
  - (b) the issuer already has debt or equity securities registered with the FSC or its equity securities are already listed for trading on a recognized stock exchange;
  - (c) the issuer is not in default of any requirements under securities legislation; and

- (d) the purchaser has access to substantially the same information concerning the issuer and its securities as if he/she had been provided with a prospectus.

4. where a private issuer distributes securities to a person who purchases the security as principal and is one of the following categories of persons associated with the issuer: director, officer, founder or controlling person of the issuer, or a close business associate of the issuer or its officers. In these circumstances however, there is a prohibition on the payment of any commission or finder's fee to any of those persons in connection with the trade of any security exempt under this head.

The FSC has reported that for the period July 17, 2008 - November 18, 2008, total securities distributed under the Guidelines amounted to J\$4.9B and US\$247M. This is a significant growth when compared with the previously stricter framework for the placement of securities. For the corresponding period in 2007, only J\$1.45B and US\$47M worth of securities were issued.

Where an issue of securities is by way of exempt distribution, the issuer must comply with the other provisions of the Guidelines and must file a Notice of Exempt Distribution within the prescribed period. Until delivery of this Notice, an issuer is prohibited from engaging in or taking any step in furtherance of any dealing relating to the relevant securities. There are also restrictions on the resale of such securities.

The expectation is that with relaxed securities regulation, such as these Guidelines, and also the anticipated introduction of less rigid requirements for listing on the Junior Market of the Jamaica Stock Exchange, many businesses will be provided with opportunities to weather these challenging times and grow.

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