



CONSULTATION PAPER NO. 98

15 SEPTEMBER 2014

PROPOSED CODE OF MARKET CONDUCT

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PROPOSED CODE OF MARKET CONDUCT

Why are we issuing this paper?

1. The Markets Law 2012 (the Markets Law) contains provisions which prohibit persons from engaging in market abuse.
2. The DFSA proposes to issue information in the form of Guidance on the market abuse regime in the Markets Law. The proposed Guidance would be included in a new standalone document called the Code of Market Conduct.
3. The Guidance proposed in the Code of Market Conduct is intended to provide further information and clarity to market participants about the market abuse regime and, in particular, to assist them:
 - (a) to determine whether or not conduct may constitute market abuse under the Markets Law;
 - (b) to avoid engaging in market abuse; and
 - (c) to clarify that certain legitimate market practices will not ordinarily amount to market abuse.

Who should read this paper?

4. The proposals in this paper would be of particular interest to:
 - (a) Authorised Firms;
 - (b) Authorised Market Institutions;
 - (c) Authorised Individuals;
 - (d) Recognised Bodies and Recognised Members;
 - (e) Issuers and Reporting Entities;
 - (f) Persons offering Investments in or from the DIFC;
 - (g) Persons investing or intending to invest in an Investment offered in or from the DIFC;
 - (h) other persons conducting or wishing to conduct activities in or from the DIFC; and
 - (i) Persons providing legal, compliance, accounting and audit services to persons referred to in (a) to (h).

How to provide comments?

5. All comments should be in writing and sent to the address or email specified below. If sending your comments by email, please use the Consultation Paper number in the subject line. You may, if relevant, identify the organisation you represent in providing your comments. The DFSA reserves the right to publish, including on its website, any comments you provide, unless you expressly request otherwise at the time of making comments.

Comments to be addressed or emailed to:

Consultation Paper No. 98
Policy and Legal Services
DFSA
PO Box 75850
Dubai, UAE

Email: consultation@dfsa.ae

Tel: +971(0)4 3621500

What happens next?

6. The deadline for providing comments on the proposals is **15 October 2014**. Once we receive your comments, we shall consider if any further refinements are required to these proposals. We shall then proceed to seek approval from our Board for the finalised proposals. Once the proposals are approved, we shall issue a notice on our website to this effect.

Terminology in this paper

7. In this paper, defined terms are identified throughout by the capitalisation of the initial letter of a word or of each word in a phrase and are defined in GLO or in the proposed amendments. Unless the context otherwise requires, where capitalisation of the initial letter is not used, the expression has its natural meaning.

How is this paper structured?

8. In this paper, we set out:
 - (a) an overview of the market abuse regime (paragraphs 9 to 13);
 - (b) the use of Codes and the reasons for the proposed introduction of a Code of Market Conduct (paragraphs 14 to 19);
 - (c) the proposed scope and legal effect of the Code (paragraphs 20 to 24);
 - (d) the content of the Code (paragraphs 25 to 27);
 - (e) application to specific market practices (paragraphs 28 and 29);
 - (f) Appendix 1 – Draft Code of Market Conduct;

- (g) Appendix 2 – Draft amendments to the MKT Module; and
- (h) Appendix 3 – Draft amendment to the Glossary Module.

An overview of the market abuse regime

9. The Markets Law sets out prohibitions against conduct known as market abuse (see Part 6 of the Law). It prohibits persons from engaging in fraud and market manipulation, disseminating false or misleading information, using fictitious devices, engaging in insider dealing, providing inside information to another person, inducing another person to deal and misusing certain information. It also defines some key concepts, such as Inside Information, and sets out a number of defences, for example, relating to price stabilisation and share buy backs.
10. The current market abuse regime was introduced in 2012 and contained a number of enhancements to the previous market misconduct regime. In particular, it was intended to align the market abuse provisions more closely with the European Union (EU) approach reflected in the Market Abuse Directive, as implemented by the UK regime.
11. While the Markets Law regime is broadly based on the UK and EU regime it does contain some differences which reflect the differing market structure and regulatory framework in the DIFC. For example, it potentially applies to a broader range of Investments, including Investments that are not admitted to an Exchange in the DIFC, and includes an additional prohibition against conduct that induces a person to deal. There are also various differences in the content of the prohibitions which were adjusted to reflect local requirements.
12. It should be noted that the market abuse regime prohibits conduct by any person whether an individual or body corporate and whether or not regulated. The regime also applies not only to conduct inside the DIFC but also to conduct which occurs outside the DIFC if that conduct affects DIFC markets or users of DIFC markets.
13. Although Part 6 of the Markets Law sets out the elements of each type of market abuse prohibition, relevant definitions and some defences, it does not provide detail about what types of conduct contravene each prohibition or about the operation of the provisions. However, the Markets Law does provide for the making of Rules for the prevention of market abuse, including a code of market conduct (see Article 8(2)(f) of the Markets Law).

Use of codes and guidance relating to market abuse

14. The use of guidance to explain or clarify the scope and effect of market abuse regimes is an approach adopted in a number of benchmarked jurisdictions.
15. For example, in the UK, the Financial Conduct Authority has issued the Code of Market Conduct. This Code sets out descriptions of behaviour that contravene the UK provisions, other types of behaviour that does not amount to a contravention and factors that the regulator may take into account in determining whether or not a contravention has occurred. Under UK legislation, the provisions in the Code have formal legal effect and create legal

presumptions. If a person engages in behaviour described in certain provisions of that Code they are *prima facie* deemed to commit market abuse or in other cases deemed not to be committing market abuse i.e. fall within a 'safe harbour'.

16. Various other benchmarked jurisdictions also adopt a similar approach of issuing further information explaining or clarifying the scope and effect of their market abuse regime. For example, the Central Bank of Ireland has issued guidance on the market abuse provisions in Ireland. Also, the proposed new EU Regulation on Market Abuse provides for the issue of standards and guidelines relating to the Regulation.

Introduction of a Code of Market Conduct

17. While Part 6 of the Markets Law generally does not require the introduction of any further Rules or Guidance in order for the market abuse provisions to be legally effective (apart from Rules setting out how price stabilisations and purchase of own shares must be carried out to fall within the relevant defences), we consider that it would be desirable to issue further information to assist market participants to understand the scope and effect of the market abuse regime.
18. We propose that this information should be in the form of Guidance on the market abuse provisions that will be contained in a new standalone module in the sourcebook called the Code of Market Conduct. This Guidance would include our view on interpretation of some provisions, examples of conduct that in our view may contravene the prohibitions and other conduct that in our view does not contravene a prohibition. It would also set out factors that we may take into account in determining whether or not conduct may be market abuse.
19. We consider that the issue of Guidance will have a number of benefits to the market such as:
 - (a) assisting persons to determine whether or not conduct is likely to amount to market abuse;
 - (b) assisting persons to monitor for and prevent market abuse and to report suspected market abuse where they are under an obligation to do so; and
 - (c) clarifying in certain cases that certain legitimate practices do not ordinarily amount to market abuse.

Issues for consideration

Q1: Do you agree with the proposal that the DFSA issue further information about the market abuse regime? Do you agree with the proposed benefits of publishing a Code? If not, please specify what your concerns are and how they might be addressed?

Scope and legal effect of the Code

20. We consider that the UK Code provides a useful precedent as the market abuse provisions introduced in the Markets Law were broadly aligned with the prohibitions in the EU Market Abuse Directive as implemented by the UK regime. We propose, therefore, to follow a similar structure, i.e. of identifying the different types of market abuse, setting out the text of the prohibition, providing our view of some elements of the provisions, providing examples of conduct that may amount to market abuse and examples of other conduct that does not amount to market abuse and including, where appropriate, factors that we may take into account in determining whether or not there may have been a contravention.
21. While we propose to adopt a similar structure to the UK Code, we propose to adapt the content to reflect differences in the legal provisions and in the nature and structure of markets in the DIFC.
22. We also propose that the legal status of the Code should differ from the UK Code and, instead, follow other benchmarks. We propose that the Code of Market Conduct should be Guidance and as such should be indicative and non-binding rather than having any formal legal effect. We believe this is more appropriate to the DIFC as:
 - (a) markets in the DIFC are at a different stage of development from those in other financial centres and, at this stage, it seems to us more important to be providing information to market participants about the effect of the market abuse regime rather than solely facilitating enforcement of the regime;
 - (b) there are differences in the nature of the market in the DIFC. For example, the DIFC does not yet have the same volume of trading or diversity of trading participants and arrangements as in other centres and to date there is no evidence of significant levels of market abuse; and
 - (c) the Markets Law does not contain the same detailed legal scheme as the UK Law which mandates the issue of a Code (after consultation) and then contains express provisions for the Code to create certain legal presumptions.

We note that although Guidance is indicative and non-binding, in our experience, courts often do take into account guidelines issued by regulators in interpreting legislative provisions.

23. The Code would be different in nature to other codes issued by the DFSA (such as, for example, Corporate Governance best practice standards or the Hedge Fund Code). In those cases the codes set out guidelines or best practice standards to achieve compliance with overarching requirements in the laws and Rules. They then require the person to 'comply or explain' if they have complied with the code. By contrast, rather than setting out how a person should comply with requirements, the Code will illustrate our view of interpretation of the market abuse regime, examples of market abuse and factors the DFSA may take into account. That is, it is to assist persons to avoid

engaging in market abuse. Therefore, we believe the Code of Market conduct would by its nature be less amenable to incorporation in Rules.

24. We propose however to make a minor amendment to the Markets Rules module to include a new section that would act as a signpost to the standalone Code of Market Conduct module and confirm that the Code has the status of Guidance (see Appendix 2).

Issues for consideration

Q2: Do you agree with the proposal that the legal status of the proposed Code of Market Conduct should be in the form of Guidance that is indicative and non-binding rather than having any formal legal effect? If not, please specify your concerns and what legal effect you believe the Code should have?

Structure and content of the Code

25. In the draft Code we set out the different types of market abuse under the Markets Law. For each type of market abuse we set out some or all of the following:
- (a) a summary of the text of the prohibition and relevant definitions;
 - (b) the DFSA's interpretation of elements of the prohibition;
 - (c) examples of generic types of conduct and/or hypothetical examples of conduct which in the DFSA's view may contravene the prohibition;
 - (d) factors the DFSA may take into account in determining whether or not a provision may have been contravened; and
 - (e) where relevant, defences that apply to the prohibition.
26. In the Code we have tried to focus on those areas where, from past experience, contraventions are more likely to occur or where we believe market participants are more likely to seek clarity about how a provision should be interpreted or how it may apply to a particular situation. In some cases, if we consider that a provision is self-explanatory or in practice is less likely to apply, we have tried to keep the Guidance relatively short.
27. Where the Code sets out examples of market abuse or factors that the DFSA may take into account in deciding whether or not conduct amounts to market abuse, the Code is not intended to be exhaustive or to try to describe every example or every factor that may be relevant. The examples and factors are intended to be illustrative and not exhaustive.

Issues for consideration

Q3: Do you have any concerns or issues relating to the specific Guidance in the draft Code of Market Conduct? Are there any issues upon which you disagree or require further clarification? If so what are those issues and why do you disagree or require clarification? Are there any other relevant examples that you believe should be included in the Code?

Application to certain market practices

28. The Markets Law already sets out a number of defences for market practices such as price stabilisation, purchase of own shares, market making, underwriting and execution of client orders. If a person complies with the conditions of those defences they will not commit market abuse. In some cases the DFSA provides further Guidance in the Code about the defences.
29. There are also other market practices that are ordinarily legitimate but which are not referred to in the Markets Law. Such practices include, for example, securities lending, repos and providing collateral or engaging in short selling. The Code sets out some DFSA guidance on these practices to clarify that they would not usually of themselves constitute market abuse.

Issues for consideration

Q4: Do you believe that the Code provides sufficient Guidance about these market practices? Are there any other areas of market practice which you consider are legitimate and upon which further Guidance could be provided?