CONSULTATION PAPER NO. 123

FUND PROTOCOL RULES

27 NOVEMBER 2018

PREFACE

Why are we issuing this consultation paper (CP)?

1. The DFSA proposes to amend its Rulebook to introduce a new facility for the marketing and sale of units of domestic funds in the UAE.

2. The method of introducing these changes is somewhat unusual. The DFSA has entered into an agreement with the Securities and Commodities Authority (**SCA**) of the UAE, and with the Financial Services Regulatory Authority (**FSRA**) of the Abu Dhabi Global Market (**ADGM**), which sets out the changes to be made. The reasons for taking this approach are discussed below.

3. This Consultation Paper seeks stakeholder views on the proposals.

Who should read this CP?

4. The proposals in this paper would be of particular interest to:
   a) Authorised Firms carrying out any one or more of the following financial services involving a domestic fund or its units:
      i) Managing a Collective Investment Fund;
      ii) Dealing in Investments as Principal;
      iii) Dealing in Investments as Agent;
      iv) Arranging Deals in Investments;
      v) Advising on Investments; and
      vi) Providing Custody;
   b) Authorised Firms that issue financial promotions relating to a domestic fund or its units; and
   c) advisers to any of the above.

Terminology

5. In this CP, other than in the Appendices, in order to improve readability of the text, a number of proposed defined terms and currently defined terms, which are used repeatedly, do not have their initial letter capitalised to identify them as defined terms.

6. In the Appendices, however, defined terms are identified by the capitalisation of the initial letter of a word, or of each word in a phrase, and are defined in the Glossary Module (**GLO**). Where capitalisation of the initial letter is not used, the expression has its natural meaning.

What are the next steps?

7. All comments should be emailed to **consultation@dfsa.ae** using the table provided in Appendix 8. Please refer to the consultation paper number in the subject line. You may 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. The deadline for providing comments is **3 January 2019**.

8. Once we receive comments, we shall consider whether any changes are required to these proposals and then seek approval from the DFSA Board for the finalised proposals. Once the proposals are approved, we shall issue a notice on our website to this effect.

Structure of this CP

9. The structure of the remainder of this paper is as follows:

Introduction	
Section 1	New proposals
Section 2	Proposed consequential changes to the existing regime
Appendix 1:	Draft Fund Protocol Rules (FPR) Module
Appendix 2:	Draft amendments to the GEN Module
Appendix 3:	Draft amendments to the CIR Module.
Appendix 4:	Draft amendments to the GLO Module.
Appendix 5:	Draft amendments to the FER Module.
Appendix 6:	Draft amendments to the MKT Module
Appendix 7:	Draft Recognised Jurisdiction Notice (No. 4)
Appendix 8:	Table for providing comments.

INTRODUCTION

10. Federal Law No. 8 of 2004 provides that entities licensed within the DIFC may conduct activities in and from the DIFC, in the broader UAE, subject to the exceptions stipulated in that Law in respect of certain activities. These limited exceptions are deposit taking, dealing in the UAE Dirham, and the conduct of insurance business apart from reinsurance. It remains the view of the DFSA that Federal Law No. 8 of 2004 permits DIFC licensed firms to do business, in all types of securities and investments, in or from the DIFC, including with clients based in the UAE outside the DIFC.

11. However, the DFSA is aware of the practical difficulties that have arisen for DIFC licensed firms in this area, including those conducting funds business, in terms of the requirements of other UAE regulators.

12. The DFSA has been in discussions with the SCA and FSRA regarding how to work together in order to make doing business as easy as possible (in the case of DIFC licensed firms, in the wider UAE outside the DIFC), by removing the existing practical difficulties, in the interests of the financial services sector in the UAE and its clients.

13. The discussions have resulted in a joint proposal to introduce a notification and registration facility for the marketing and sale of units in domestic funds and the conduct of associated financial services. Although the current proposals are limited to domestic funds, the DFSA intends to seek the agreement of the other regulators to expand the proposals in the future to include other financial products to assist DIFC licensed firms to overcome or mitigate any other practical difficulties of doing business from the DIFC in the broader UAE.

14. The proposed notification and registration facility will enhance regulatory co-operation between the three securities regulators with regard to qualifying domestic funds being promoted within the UAE. It is proposed to set out the framework for this special facility in a new module of the DFSA Rulebook: the Fund Protocol Rules (**FPR**) module. This is attached as Appendix 1.

15. The proposed facility will be of particular interest to fund managers of domestic funds, but also of interest to other authorised firms that propose to carry on, or are carrying on, the marketing and selling of the units of such funds to potential investors and clients situated in the UAE, outside the DIFC.

Key features of the proposed facility

Please see the proposed changes in FPR at Appendix 1

16. The proposals retain the fundamental principle of "single licence" and single regulatory and legislative regime for conducting financial services in the UAE. The proposed facility will sit alongside the current collective investment regime, which will continue to apply, unless stated otherwise, to those persons specified under the Collective Investment Law (DIFC Law No. 2 of 2010) and CIR Rules. The proposed facility only affects the marketing of, and any financial services carried on involving, domestic funds and their units, for those firms which choose to opt in to it.

17. For example, DIFC firms which currently use a SCA-authorised distribution agent to distribute the units of domestic funds in the UAE

outside the DIFC, may decide instead to opt in to the proposed facility and market and distribute the units themselves.

18. There are a number of important terms used in this section of the paper which are as follows:

a) home jurisdiction – the jurisdiction in which the fund manager is licensed and the fund domiciled;

b) home regulator – the financial services regulator that issues the licence referred to above;

c) host jurisdiction – the jurisdiction, other than the home jurisdiction, in which marketing and sales of units will take place; and

d) host regulator – the financial services regulator in the host jurisdiction.

In addition, it should be noted that "promotion" includes not only the marketing and sale of units, but also the carrying on of certain related financial services such as advising, dealing and arranging in relation to the units.

The above terms, and other new terms used in the FPR module, are more fully defined in the table in section 1.3 of that module.

SECTION 1 NEW PROPOSALS

1. Registration

Please see the proposed FPR Rules 3.1.2 to 3.1.7, 3.2.2 to 3.2.7, and 7.1.2 at Appendix 1

19. A fund manager of a DIFC domestic fund can opt in to the facility. If it does so, it must notify the DFSA of the domestic fund it wishes to register and pay the required notification fee. The fund manager's notification to the DFSA must include various details relating to the domestic fund and include a copy of the fund's prospectus or offering document (and in some cases the key investor information document – see paragraph 25 below).

20. Provided it meets all the requirements, the fund would then be registered by the DFSA, which will notify the host regulator(s). The host regulator(s) will then include the fund on their own register of funds.

21. Once the domestic fund is registered, the fund manager will be able to promote units of the fund in the host jurisdiction(s) without meeting any other administrative or regulatory requirement, in particular those of the host regulator(s), except as specified below.

22. The DFSA has various duties regarding the register and these are set out under Chapters 4 and 5 of the FPR.

2. Custodians

Please see the proposed FPR Section 6.5 at Appendix 1

23. Under the proposals, if the domestic fund to be registered is a public fund, it must appoint a custodian which is licensed by the SCA, unless the public fund is a property fund. Sub-custodians can still be appointed by the custodian. This requirement is intended to assist in the development of this segment of the financial services industry within the UAE, outside the DIFC.

3. Prospectus and Key Investor Information Document

Please see the proposed FPR Rules 3.1.3, 3.2.3 and App 1 at Appendix 1, CIR Rules 14.2.1(4), 14.3.1 and 14.3.3 at Appendix 3, and MKT Rule 6.3.1 at Appendix 6

24. It is also proposed to introduce in the prospectus additional standardised text for inclusion in the disclaimers for both public and private funds. This requirement is intended to provide alignment with the SCA and FSRA regimes.

25. If the registered fund is a public fund, it is proposed that the fund manager must, in addition to the prospectus, provide a key investor information document in English and Arabic. This requirement is intended to enhance understanding of the prospectus by potential investors within the UAE and follows similar requirements imposed in the European Union mandating the provision of a summary of the key information separately from the detailed prospectus.

4. Host jurisdictions

Please see the proposed FPR Rules 3.1.3 and 3.2.3 at Appendix 1

26. Where the DIFC is the home jurisdiction of a Fund, the fund manager will need to decide whether it wants to promote to potential investors and clients in either or both of the following host jurisdictions:

a) the UAE outside the DIFC and the ADGM; and

b) the ADGM.

5. Notification by the DFSA

Please see the proposed FPR Rules 3.1.4 to 3.1.6 and 3.2.4 to 3.2.6 at Appendix 1

27. Under the proposals, the DFSA will notify the registration of the domestic fund, to the relevant host regulator(s) of the jurisdiction(s) into which the promotion of units will be conducted.

28. The proposals also specify when the DFSA, as the home regulator, may decide not to register and provide notification to the other authorities. This includes, for example, when the DFSA has reason to believe that the fund manager is not complying with applicable legislation.

6. Financial services in or from the DIFC

Please see the proposed FPR Rules 3.1.7 and

29. Once registered under the proposed facility, financial services, including advising, arranging and dealing, may be conducted or continue to be conducted in respect of the fund's units, with or for

3.2.7 at Appendix 1

investors and clients in the chosen host jurisdiction(s) by any appropriately authorised firm.

7. Applicable legislation

30. In regard to applicable legislation, the DFSA administered legislation will continue to apply to authorised firms with respect to financial services conducted with or for any person, whether that person is situated within the DIFC or elsewhere in the UAE.

8. De-registration

Please see the proposed FPR Section 8.1 at Appendix 1

31. Section 8.1 of the FPR Rules specifies the circumstances in which the DFSA may de-register a domestic fund, such as upon request by the fund manager or upon commencement of winding-up of the fund.

9. Supervisory and enforcement action

Please see the proposed FPR Rules 9.1.1 to 9.2.3 at Appendix 1

32. The FPR Rules describe the circumstances in which the DFSA:

    a) may request a host regulator to assist in the conduct of an investigation relating to the activities of the fund manager or other licensed persons in the host jurisdiction; or

    b) would permit a host regulator to undertake a joint supervisory inspection with the DFSA of a fund manager in the DIFC.

Please see the proposed FPR Rules 9.4.1 to 9.4.4 at Appendix 1

33. The FPR Rules also describe some of the factors that the DFSA (as home regulator) would take into account before exercising any of its powers at the request of a host regulator in relation to the promotion of a fund.

34. None of the above mentioned provisions fetter in any way the DFSA's exercise of its powers under the laws it administers.

SECTION 2 PROPOSED CONSEQUENTIAL CHANGES TO THE EXISTING REGIME

35. In addition to introducing a new module of rules, it is also proposed to make consequential amendments to the GEN, CIR, MKT, GLO and FER modules as described below.

1. GEN Amendments

Please see the proposed changes to GEN Rules

36. The amendments to GEN are to clarify that, where the DIFC is the host jurisdiction, a fund manager, its agent or a licensed person authorised in the home jurisdiction may promote the registered fund in the DIFC without requiring a) additional DFSA authorisation or b) any additional approvals for a financial promotion.

2.3.6 and 3.5.1 at Appendix 2

37. Under the proposed FPR, the requirements of the home jurisdiction will apply to such a promotion. Further, the home regulator is primarily responsible for taking action if there is a contravention of those requirements.

2. CIR Amendments

38. A number of amendments are made to CIR to implement the proposals.

Please see the proposed changes to CIR Rule 4.1.5 at Appendix 3

39. First, an offer of a unit of a registered fund in the DIFC, where the DIFC is the host jurisdiction, is specified to be an excluded offer. This is necessary because the offer of the units in the fund will be subject to the requirements of the home jurisdiction relating to a prospectus and marketing. It is, therefore, unnecessary to apply duplicative requirements in the host jurisdiction.

Please see the proposed changes to CIR Chapter 15 at Appendix 3

40. In addition, various changes are proposed to permit authorised firms in the DIFC to offer units of a registered fund (where the DIFC is the host jurisdiction). This will ensure that DIFC authorised firms are able to promote units of a registered fund in the DIFC (should they choose to do so) in the same way as the fund manager, its agent or a licensed person from the home jurisdiction.

Please see the proposed changes to CIR Section 1.5 and CIR Rules 8.2.4, 8.2.5, 14.2 and 14.3 at Appendix 3

41. Finally, under the proposals, if a fund established or domiciled in the DIFC wishes to be a registered fund it must, in addition to the normal DFSA requirements, meet certain additional requirements specified in the proposed FPR, as discussed in Section 1. The CIR Rules are amended in a number of places for consistency with additional, or modified, requirements specified in the proposed FPR.

<u>Recognised Jurisdiction Notice</u>

Please see the proposed Recognised Jurisdiction Notice (No. 4) at Appendix 7

42. As set out above for the proposed amendments to CIR Chapter 15, there is currently a restriction on authorised firms in the DIFC offering units in a foreign fund. To permit DIFC authorised firms to also offer units of a fund that is registered under this facility, the DFSA proposes to designate domestic funds, for which the SCA or the FSRA is the home regulator, to be “Designated Funds” from a “Recognised Jurisdiction”.

3. MKT Amendments

Please see the proposed changes to MKT Rule 6.3.1 at Appendix 6

43. As mentioned in paragraph 24, under the proposals, additional disclaimers are to be included in the prospectus of a public fund. The consequential amendments in MKT reflect these changes for listed funds.

4. GLO Amendments

Please see the proposed changes to GLO at Appendix 4 and FPR Section 1.3 at Appendix 1

44. GLO is amended to include a number of key definitions from the proposed new FPR. These changes include definitions of 'Passported Fund', 'Home Regulator', 'Host Regulator', 'Home Jurisdiction', 'Host Jurisdiction', 'Promote', 'Agent' and 'Licensed Person'. Many of these definitions cross refer to the definitions used in the proposed new FPR.

5. FER Amendments

Please see the proposed changes to FER Rules 1.2.2, 2.5.1 and 3.10A at Appendix 5, and Chapter 7 of the proposed FPR at Appendix 1

45. The proposals provide for fees to be paid to the home regulator where a domestic fund uses the new facility. First, a notification fee of USD 9,500 is payable when a fund manager notifies the home regulator of its intention that a domestic fund be a registered fund. Then, an annual fee of USD 2,000 is payable each year in respect of the registered fund. For an umbrella fund or a segregated portfolio company or cell company, the fee is calculated per sub-fund, segregated portfolio or cell (as the case may be).

Questions:

Q1. Would you use, or need to use, the proposed facility? Alternatively, have you arranged your business affairs so that the proposed facility would not benefit your business in the UAE?

Q2. If you would use the proposed facility, please could you comment on the expected impact of the proposed changes on your activities? If you have any concerns, what are they and how should they be addressed?

Q3. In respect of public funds which are not property funds, is the proposal to make it mandatory for such funds to appoint an SCA authorised custodian likely to cause any issues? If so, please provide details.

Q4. Regarding the notification fees, would these cause any issues, in particular regarding your sales of units?

Q5. Do you have any other comments on the proposals?

Appendix 8: Table of Comments

Name of commentator:		
Name of entity (if applicable)		
Is your response confidential?	☐ Yes	☐ No
If your response to the previous question is Yes, please state your reasons for such a request:		

Notes:

- The DFSA reserves the right to publish, including on its website, any comments you provide. However, if you wish your comments to be kept confidential, you must expressly request at the time of making comments that this should be the case. You must also provide an explanation of why you wish your comments be kept confidential.
- Your answers may require explanations. Please include those in the second column.
- If you do not wish to comment on any issue, please select the "no comments" box.

Ref.	Response	Comments on proposal	
Q1:	**Would you use, or need to use, the proposed facility? Alternatively, have you arranged your business affairs so that the proposed facility would not benefit your business in the UAE?**		
	☐ Yes ☐ No	Click here to enter text.	☐ No comments
Q2:	**If you would use the proposed facility, please could you comment on the expected impact of the proposed changes on your activities? If you have any concerns, what are they and how should they be addressed?**		
	☐ Yes ☐ No	Click here to enter text.	☐ No comments
Q3:	**In respect of public funds that are not property funds, is the proposal to make it mandatory for such funds to appoint an SCA authorised custodian likely to cause any issues? If so, please provide details.**		
	☐ Yes ☐ No	Click here to enter text.	☐ No comments
Q4:	**Regarding the notification fees, would these cause any issues, in particular regarding your sales of units?**		
	☐ Yes ☐ No	Click here to enter text.	☐ No comments
Q5:	**Do you have any other comments on the proposals?**		
	☐ Yes ☐ No	Click here to enter text.	☐ No comments