



CONSULTATION PAPER NO.28

4 MAY 2006

**THE PROPOSED RESTRUCTURING OF THE ANCILLARY SERVICE
PROVIDERS REGIME**

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Why are we issuing this paper?

1. This Consultation Paper sets out the DFSA's proposals to restructure the Ancillary Service Providers Regime (the ASP regime) for public comment. These proposals encompass retaining the ASP regime only in relation to persons providing legal and accounting services in and from the DIFC and removing its application to the other four categories of Ancillary Service Providers ("ASPs"), i.e. Compliance Services, Market Information Services, Management Offices and Local Services Offices ("LSOs"). However, marketing and promotion of financial services, the kind of activities currently conducted by LSOs, would be subject to regulation as a Financial Service and, therefore, require authorisation.
2. These proposals reflect the DFSA's risk based approach to regulation and form part of a package of proposals aimed at reducing unnecessary compliance process and regulatory costs. The proposals are contained in Consultation Papers No. 28 to 32, which are being released for public comment at the same time.

Who should read this paper?

3. The proposals in this paper would be of primary interest to persons who are currently registered or intend to be registered as an ASP. They will also be of interest to Authorised Firms which conduct Financial Services that include financial promotion activities and marketing activities and also, Authorised Firms that use ASPs providing legal or accounting services.

How is this paper structured?

4. In this paper, we set out:
 - (a) defined terms in paragraph 7;
 - (b) scope and purpose of the proposals in paragraphs 8 and 9;
 - (c) details of the proposed changes to the ASP Module in paragraph 10;
 - (d) details of the proposed changes relating to financial promotion in paragraphs 11 – 14;
 - (e) transitional arrangements in paragraphs 15 and 16; and
 - (f) a specific issue on which we seek comment in paragraph 17.

How to provide comments

5. All comments should be provided to the person specified below. 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.

What happens next?

6. The deadline for providing comments on these proposals is 2nd June 2006. Once we receive your comments, we will consider if any further refinements are required to these proposals. We will then proceed to enact the changes to the DFSA's Rulebook. You should not act on these proposals until the relevant changes to the DFSA Rulebook are made. We will issue a notice on our website telling you when this happens.

Comments to be addressed to:

Roberta Julfar
Legislative Counsel
DFSA
PO Box 75850
Dubai, UAE

or e-mailed to rjulfar@dfsa.ae

Defined Terms

7. The terms used in this paper have the same meaning as in the Rulebook Glossary, unless otherwise stated. For convenience of reference, in this Paper:
- (a) 'ASP' means an Ancillary Service Provider;
 - (b) 'ASP regime' means the regulation under the current ASP Module;
 - (c) a 'regulated entity' means an Authorised Firm, Authorised Market Institution or and Ancillary Service Provider;
 - (d) 'AML' means anti money laundering regulation and includes the regime under the AML Module;
 - (e) 'Advising' means the Financial Service of 'Advising on financial products or credit';
 - (f) 'Arranging' means the Financial Service of 'Arranging credit or deals in Investments'
 - (g) FATF means Financial Action Task Force; and
 - (h) LSO means a Local Services Office.

Scope and purpose of these proposals

8. There are three key elements to the proposed ASP restructure:
- (a) Remove the requirement for registration in relation to four categories of ASPs. These categories are operators of Compliance Services, Market Information Services, Local Services Offices and Management Offices;
 - (b) Retain the ASP regime for the remaining two categories of ASPs, i.e. providers of Legal Services and Accountancy Services to 'regulated entities' (i.e. Authorised Firms, Authorised Market Institutions and Ancillary Service Providers) but reduce its scope to focus on AML; and
 - (c) Regulate financial promotion and marketing activities of the kind currently conducted by LSOs as a Financial Service.
9. The objectives of these proposals are:
- (a) to remove the unnecessary regulatory burden on the operators of Compliance Services, Market Information Services and Management Offices. This is because these services are truly support services. By their very nature, they do not pose any significant risks to Financial Services provided in and from the DIFC;
 - (b) to ensure that Legal Services and Accountancy Services provided to regulated entities remain the subject of regulation under the ASP regime. This is to address possible money laundering risks that can arise in the context of the provision of these professional services, which could tarnish the reputation of regulated entities and consequently, the DIFC as a whole; and
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- (c) to regulate financial promotion and marketing activities of the kind conducted by LSOs through clarified boundaries of the relevant Financial Services. This approach would result in increased costs to persons carrying on financial promotion and marketing activities. For example, they would be required to pay an authorisation fee of US\$10,000, as opposed to the ASP registration fee of US\$2,000, as well as increased annual fees. However, the DFSA considers this approach to be consistent with its risk based approach to regulation, particularly as most of the financial promotion and marketing activities are in essence an integral part of the provision of Financial Services and hence warrant regulation as a Financial Service to promote consistent regulation. This also promotes clarity and certainty for persons conducting these activities.

Details of the proposed changes to the ASP regime

- 10. The proposed key changes to the ASP regime consist of the following:
 - (a) removal of the Compliance Services, Market Information Services, LSOs and Management Offices as categories of ASPs for reasons set out in paragraph 3(a) above;
 - (b) deletion of:
 - i. the Code for Ancillary Service Providers in Chapter 4 of the ASP Module which is no longer necessary in light of the fact that the regime is geared only to address anti money laundering risks;
 - ii. notification requirements relating to annual declaration of compliance and solvency and controllers;
 - iii. the requirement for lawyers and accountants to be members of professional bodies; and
 - iv. the requirement of a designated Principal Representative;
 - (c) the removal of the need to be registered as an ASP before being able to solicit clients and market their services to prospective clients. As a result, accounting and legal firms that propose to be registered as an ASP will be able to solicit clients and market their services in the DIFC subject to other applicable requirements in the DIFC but must obtain registration as an ASP before providing their services to a regulated entity. For obtaining registration as an ASP, they should be able to produce some evidence of intent by a regulated entity to use their services; and
 - (d) the refinement of the anti money laundering provisions in the ASP Module (i.e. in chapter 7) to provide greater clarity as regards what is required of the two remaining categories of ASPs as above whilst still ensuring that FATF requirements are fully incorporated.

(See Annex A containing the draft amendments to the ASP Module)

Details of the financial promotion related proposals

11. Activities conducted by LSOs, for which they require registration as an ASP under the current ASP regime, are defined in Rule 2.3.4 as follows:
 - (a) seeking, or offering generic advice to, potential customers with a view to the provision of financial services, either directly or by a member of the same Group, from an establishment outside the DIFC; and
 - (b) marketing and other activities relating to (a) but not amounting to Financial Services in GEN Chapter 2.

 12. The financial promotion and marketing activities conducted by LSOs within the boundaries set by the above definition include:
 - (a) developing client relationships and servicing client needs to support head office functions;
 - (b) providing a point of contact to local clients;
 - (c) promoting the profile of the head office by giving generic advice about the financial services offered by the head office or other profile raising promotional work (e.g. sponsorships of local events and use of logo in billboard advertising);
 - (d) seeking out potential customers and making referrals of them to the head office; and
 - (e) reporting to the head office on business and market trends.

 13. Most of the activities of the kind described above are generally conducted as an integral part of providing the Financial Services of Arranging and Advising or Insurance Intermediation. We propose to amend the relevant definitions as follows to ensure that financial promotion and marketing activities are clearly brought within those definitions:
 - (a) The definition of 'Arranging credit and deals in Investments' in Rule 2.9 of GEN is to be amended to explicitly include the activities of making invitations and engaging in any other conduct that is intended or capable of influencing customers or potential customers to enter into transactions relating to financial products and obtaining credit;
 - (b) The definition of 'Advising on financial products or credit' in Rule 2.11 of GEN is to be amended to include giving 'generic advice' about financial products or credit, which is directly or indirectly intended to influence customers and potential customers when making decisions relating to financial products and credit to which the advice relates; and
 - (c) The definition of 'Insurance Intermediation' in Rule 2.10 of GEN is also amended to capture the extended meanings of 'Arranging' and 'Advising' as set out in (a) and (b) above, in relation to insurance contracts and insurance cover.
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14. Taking into account the nature of risks associated with the Financial Services referred to above, we also propose to reduce the fixed initial capital component of the base requirement for Firms in Category 4 as defined in the PIB Module from \$250,000 to \$10,000. The proposed requirement for such a Firm would then be \$10,000 or 6/52 of the annual expenditure, whichever is the higher.

[See Annex B for draft amendments to GEN, COB, AUT and PIB Modules.]

Transitional arrangements

15. Until the enactment of the relevant legislation relating to these proposals following public consultation (i.e. during the interim period), the DFSA will adopt the following procedures:
- (a) The DFSA will only consider for registration as ASPs persons proposing to provide Legal or Accounting Services. Upon registration, those persons must comply with the current ASP requirements until any amendments to the ASP regime are made;
 - (b) The DFSA will give other persons affected by these proposals temporary relief as appropriate; and
 - (c) The DFSA requires every person currently registered as an ASP to comply with the current ASP requirements in the interim period.
16. In the case of ASPs who may not need registration after the implementation of these proposals, i.e. operators of Compliance Services, Market Information Services and Management Offices, we will consider a request for a refund of the annual fees after the implementation of these proposals. No refunds will be considered during the interim period.

Specific issue on which we seek your comment

17. We seek your comments on any aspects of these proposals including specific amendments to the DFSA Rulebook that are proposed. We also seek your comments on the specific issue whether the DFSA should dispense with the requirement for registration as an ASP where the Person is an Authorised Firm. The DFSA proposes to amend Article 44 of the Regulatory Law to permit an Authorised Firm to carry on an Ancillary Service without having to register as an Ancillary Service Provider.