



CONSULTATION PAPER NO. 30

4 MAY 2006

PROPOSED CHANGES RELATING TO SPONSORS

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Why are we issuing this Consultation Paper?

1. This Consultation Paper seeks public comment on the DFSA's proposal to revise the mandatory sponsorship regime prescribed in the Markets Law 2004 and the OSR Module of the DFSA Rulebook. In summary the DFSA is proposing to:
 - (a) retain the mandatory requirement to appoint a sponsor for Persons who make or intend to make a Prospectus Offer of Securities in the DIFC;
 - (b) clarify the regulatory obligations of a sponsor;
 - (c) eliminate the mandatory requirement to appoint a sponsor for a Reporting Entity to assist it to comply with its continuing regulatory obligations;
 - (d) give the DFSA the discretion to require a Reporting Entity to appoint a compliance adviser where the DFSA considers it necessary to assist the Reporting Entity to comply with its continuing regulatory obligations
 - (e) confirm that the responsibility for the Reporting Entity to comply with its continuing regulatory obligations remains the sole regulatory responsibility of the Reporting Entity and that the compliance adviser's role is based on contractual obligations to the Reporting Entity and not on any regulatory obligations
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 will be of primary interest to Persons who make or intend to make a Prospectus Offer of Securities in the DIFC and entities that are likely to act as their sponsors and to Reporting Entities and entities that are likely to act as their compliance advisers.

How is this paper set out?

4. In this paper, we set out:
 - (a) Defined terms in paragraph 7;
 - (b) Scope and purpose of the proposals in paragraphs 8 to 17;

- (c) Details of the proposed changes in paragraphs 18 to 31;
- (d) Issues on which we seek your comments in paragraph 32;
- (e) Index of proposed changes to the OSRs, **Annex A**;
- (f) Draft *Policy Statement on Sponsors*, **Annex B**;
- (g) Draft *Policy Statement on Compliance Advisers*, **Annex C**;
- (h) Amended OSRs, **Annex D**.

How to provide comments?

5. All comments should be forwarded 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 3 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 www.dfsa.ae telling you when this happens.

Comments to be addressed to:

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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) **Prospectus Offer** means an Offer of Securities in circumstances where a Prospectus has been filed with the DFSA and published.
 - (b) **Person** means any natural person, Body Corporate or body unincorporated, including a legal person, company, Partnership, unincorporated association, government or state.
 - (c) **Issuer** means
 - (1) in relation to any Security, other than a Unit in a Collective Investment Fund, the Person by whom the Security is or is to be issued;
 - (2) in relation to a Unit in a Collective Investment Fund, the operator of the fund;
 - (3) in relation to an interest in a limited Partnership, the Partnership; and
 - (4) in relation to Certificates, the Person who issued or is to issue the Security to which the Certificate or other instrument relates.
 - (d) **Offeror** means a Person who makes an Offer of Securities.
 - (e) **Reporting Entity** means
 - (1) Subject to (2), a person is a Reporting Entity if:
 - (i) the person has or had Securities admitted to an Official List of Securities at any time;
 - (ii) the person has filed a prospectus with the DFSA under Article 15;
 - (iii) the person merges with or acquires a Reporting Entity; or
 - (iv) the person is declared in writing to be a Reporting Entity by the DFSA.
 - (2) A person is not a Reporting Entity if:
 - (a) the person is a properly constituted government, a government agency, a central bank or other type of national monetary authority of a country or jurisdiction, a supra-national organisation whose members are either countries, central banks or national monetary authorities, a public authority or a state investment body; or
 - (b)
 - (i) the person previously had Securities admitted to an Official List of Securities;
 - (ii) the person currently has no Securities admitted to an Official List of Securities; and

- (iii) the current holders of at least 75% of voting rights in the Reporting Entity have agreed in writing that the person is no longer a Reporting Entity; or
 - (c) the DFSA so determines.
- (f) **OSRs** means the Offered Securities Rules Module of the DFSA Rulebook.

Scope and purpose of these proposals

8. The current sponsorship regime prescribed in the Markets Law and the OSR Module of the DFSA Rulebook has two parts. The first relates to the requirement to appoint a sponsor for Prospectus Offers made in the DIFC. The second relates to the requirement to appoint a sponsor for a Reporting Entity to help it comply with its continuing regulatory obligations. Part 4 of the Dubai International Financial Exchange (DIFX) Listing Rules requires an applicant for a Listing to appoint a sponsor. Nothing in these proposed amendments affect the DIFX requirements.
9. For a Prospectus Offer, the requirement to appoint a sponsor is in Rule 4.2.6 of the OSRs. It requires a Person who makes or intends to make a Prospectus Offer to appoint a sponsor in sufficient time to enable the sponsor to comply with the requirements relating to sponsors prescribed in Chapter 10 of the OSRs.
10. For Reporting Entities, the requirement to appoint a sponsor is in Rules 8.4.3 and 10.4.1 of the OSRs. They require a Reporting Entity to appoint a sponsor to ensure that the Reporting Entity complies with its continuing obligations in the Markets Law 2004 and OSRs.
11. The purpose of mandatory sponsors for Prospectus Offers was to ensure that a Person who makes or intends to make a Prospectus Offer in the DIFC is aware of, and complies with, the requirements under the Markets Law 2004 and Rules. The same rationale drove the obligation on a Reporting Entity to have a sponsor with respect to its continuing obligations. However, the appointment of a sponsor was not intended to shift the regulatory obligations of the Person making the Prospectus Offer or of the Reporting Entity onto the sponsor. These regulatory obligations are, and were intended to remain, the responsibility of the Person making the Prospectus Offer and of the Reporting Entity.
12. Nonetheless, industry stakeholders indicate that Rule 10.4.1, which states that a sponsor must ensure that a Reporting Entity complies with any applicable provisions in the Markets Law and OSRs, is being interpreted as imposing strict regulatory liability on a sponsor. While a sponsor has regulatory obligations of its own under the current regime which may properly expose it to regulatory liability, the intention was not to impose strict liability on the sponsor in circumstances where the sponsor has taken all reasonable steps to ensure that the Reporting Entity complied with its obligations but the Reporting Entity nonetheless failed to do so. This intent is reflected in the duty of care requirement in Article 10.5.1 of the OSRs.
13. In addition to the potential of strict liability, industry stakeholders expressed concern that sponsors would out of necessity become directly involved in the

daily activities of a Reporting Entity in order to effectively monitor and ensure that the Reporting Entity complies with its regulatory obligations. Stakeholders believe that if a sponsor was required to take this on properly, it would be financially prohibitive and consequently few wish to take it on.

14. Furthermore, the DFSA recognized that it was important not to have a scheme that purported to give the governing body of the Reporting Entity an excuse to shed, or transfer to the sponsor, its primary responsibilities. That said the DFSA also recognized that there may be circumstances in which certain Reporting Entities need assistance to help them meet their continuing regulatory obligations. We believe that it is in the interests of the DIFC capital markets that the DFSA be given the necessary regulatory tools and discretion to deal with these situations.
15. As a consequence, the DFSA is proposing to revise the sponsorship regime to eliminate the mandatory obligation on a Reporting Entity to appoint a sponsor to ensure the Reporting Entity complies with its continuing obligations. We are also proposing to give the DFSA the discretion to appoint, or direct a Reporting Entity to appoint, a compliance adviser to fulfil this function where the DFSA had concerns about the governance of a particular Reporting Entity or considers it otherwise necessary.
16. However, unlike the previous obligations on a sponsor, the compliance adviser's obligations would not flow from the Markets Law 2004 or OSRs but be founded in the contractual relationship between the Reporting Entity and compliance adviser. In other words, a compliance adviser would not be exposed to any potential regulatory liability under the Markets Law 2004 and OSRs.
17. Considering their function and role, the DFSA expects sponsors and compliance advisers to be properly qualified to discharge their duties. To explain the DFSA's expectations in this regard the DFSA is publishing for comment draft Guidance in the OSRs in the Chapters relating to sponsors and compliance advisers in addition to two draft policy statements.

Details of the proposed changes

Re: Sponsors

18. The following proposed amendments clarify the existing provisions and make them consistent with the overall regime change.
19. The application of Rule 4.2.6 is restricted so that the appointment of a sponsor is obligatory only for a Person making or intending to make a Prospectus Offer in the DIFC. Rule 4.2.6 is amended to clarify that the sponsor's appointment remains in effect only for the period the Prospectus Offer remains open. This means that when the Offer period ends, the mandatory sponsorship will end.
20. The term "Undertaking" in chapter 10 of OSRs is replaced with "Person" to be consistent with OSR Rule 4.2.6, which requires a "Person" making or intending to make a Prospectus Offer to appoint a sponsor.
21. Regarding a sponsor's obligations in relation to a Prospectus Offer, Rule 10.3.1(a) is amended to replace "the Offeror of the Securities" and "the

- Offeror” with “Person who makes or intends to make a Prospectus Offer”. This means, a sponsor must take reasonable steps to satisfy itself that the Person making a Prospectus Offer satisfies all applicable conditions for the Offering of Securities.
22. Rule 10.3.1(b) is amended to add “Offeror” along with an “Issuer” to capture the circumstances where the Offeror of the Securities is not the Issuer of the Securities. This means a sponsor must provide to the DFSA any information the DFSA may require for verifying that the OSR module is being complied with by both the Offeror and Issuer. Previously, the requirement related only to the Issuer.
 23. Rule 10.4.1(1), which provides that a sponsor must ensure that a Reporting Entity complies with any applicable provisions in the Markets Law 2004, is deleted. This removes the mandatory obligation to appoint a sponsor relating to a Reporting Entity’s continuing obligations and any suggestion of strict liability.
 24. The term “Undertaking” is replaced” with “Offeror and Issuer” in Rule 10.6.2 to ensure that in circumstances where the Offeror of the Securities is not the Issuer of the Securities both entities must cooperate with the sponsor and is now numbered as Rule 10.5(2). This will mean that a sponsor must notify the DFSA of any non-cooperation by the Offeror, Issuer or their Employees. The amendment clarifies that all relevant parties must cooperate with the sponsor in carrying out its obligations.
 25. The Guidance for Sponsors is amended to indicate that the DFSA will publish a *Policy Statement on Sponsors*, attached as **Annex B**, to explain in greater detail the role and regulatory obligations of a sponsor and the kind of skills, knowledge, experience, qualifications and resources the DFSA expects a sponsor to have. The Guidance explains that although a sponsor has certain regulatory obligations of its own, as prescribed in the OSR module, its principal role is to assist a Person making a Prospectus Offer to comply with its regulatory responsibilities relating to the Offer. It confirms that a Person making a Prospectus Offer does not, and cannot, avoid or diminish its regulatory obligations related to the Offering of Securities simply because it is required to have a sponsor. It emphasizes that the regulatory obligations of the Person making the Prospectus Offer are not transferred to the sponsor but remain the responsibility of the Person making the Offer.
 26. The following words have been deleted from the Guidance: “In exceptional circumstances, in light of skills, qualifications and experience of staff within the Reporting Entity, the DFSA may grant a waiver or modification of the requirement of the appointment of a sponsor.” This deletion does not affect the DFSA’s general power to grant waivers or modifications under the Markets Law 2004 and OSRs.

Re: Reporting Entities and compliance advisers

27. The reference to “sponsor” in Article 32(3) of the Markets Law 2004 is replaced with the term “compliance advisor”.

28. Rule 8.4.3(1) is amended to give the DFSA the discretion to require a Reporting Entity to appoint a compliance adviser for a specified period for the purpose of assisting the Reporting Entity to meet its continuing obligations. Rule 8.4.3 (2) is amended to provide that it is the Reporting Entity's obligation to ensure the compliance adviser continues to fulfil its role until the DFSA advises the Reporting Entity that the compliance adviser is no longer required. Rule 8.4.3(3) is deleted to achieve a unified regime rather than carving out certain exclusions for specific Reporting Entities or circumstances.
29. The new Chapter 11 *Compliance Advisers* only applies to Reporting Entities that are required to appoint compliance advisers under Rule 8.4.3. The Guidance for this Chapter emphasizes that the purpose of the compliance adviser is to assist the Reporting Entity to comply with its continuing obligations under the Markets Law 2004 and OSRs. The Guidance indicates that the DFSA's *Policy Statement on Compliance Advisers*, attached as **Annex C**, will describe in greater detail the purpose of a compliance adviser, expected knowledge, experience, qualifications and resources and the circumstances in which the DFSA is likely to require a Reporting Entity to appoint a compliance adviser.
30. The Guidance also emphasises that the compliance adviser does not take on any regulatory obligations or potential regulatory liability of its own if it agrees to act as a compliance adviser to a Reporting Entity. It confirms that the relationship between the Reporting Entity and compliance adviser is a contractual one similar to one with any other professional adviser. The compliance adviser role is merely to advise and assist the Reporting Entity to comply with its continuing regulatory responsibilities, all of which remain the responsibility of the Reporting Entity.
31. All of the obligations in the new Chapter 11 Rules dealing with compliance advisers fall on the Reporting Entity. This is reflected in Rules 11.2.2, 11.3, 11.4 and 11.5. Under these provisions it is the obligation of the Reporting Entity, who has been directed by the DFSA to appoint a compliance adviser, to:
 - (a) take reasonable steps to ensure that the compliance adviser has the required knowledge, experience, qualifications and resources to carry out its duties;
 - (b) take reasonable steps to ensure that the compliance adviser is independent and has managed conflicts of interest appropriately;
 - (c) ensure the Reporting Entity and its employees cooperate with the compliance adviser and do not interfere with the compliance adviser's ability to discharge its duties;
 - (d) take reasonable steps to rectify any failure brought to the Reporting Entity's attention by the compliance adviser;
 - (e) take reasonable steps to ensure that the compliance adviser cooperates in any investigation conducted by the DFSA as provided by OSR Rule 11.3.3; and

- (f) promptly advise the DFSA in writing when a compliance adviser resigns or is terminated including providing details of all relevant facts and circumstances.

Issues on which we seek your comment

- 32. Is the scope and content of the Rules relating to sponsors and compliance advisers appropriate?

Annex A

Index of proposed changes to OSR

Rule No.	Subject	Change
Rule 4.2.6	Mandatory appointment of a sponsor	Revised, new Rule 4.2.6(2) sets the duration of a mandatory sponsorship
Rule 8.2.3(1)(a)	Authorised disclosure	Revised, a Reporting Entity can disclose confidential information to its compliance adviser
Rule 8.4.3(1) and (2)	Appointment of a compliance adviser	Revised, the appointment is at the DFSA's discretion
Rule 8.4.3(3)	Exclusion of a mandatory sponsor for a Person who becomes a Reporting Entity by solely being admitted to the Official List in relation to Designated Investments	Deleted
Rule 10.1 and Guidance	Application of Chapter 10 on Sponsors	Revised, the word "Undertaking" is replaced with "Person". Guidance is revised.
Rule 10.2 and Rule 10.2.1(1)(c)	Appointment of a sponsor	Revised, the word "Undertaking" is replaced with "Person" in Rule 10.2. Rule 10.2.1(1)(c) deleted
Rule 10.3	Obligations of a sponsor	Revised. The word of "Person who makes or intends to make a Prospectus Offer" is replaced with "Offeror of Securities" in Rule 10.3.1(a). The word "Offeror" is added to Rule 10.3.1(b)
Rule 10.4(1)	Obligations in relation to Reporting Entities	Deleted to clarify that there is no strict liability imposed on a sponsor

Rule No.	Subject	Change
Rule 10.5 and Rule 10.6	Duty of care & Co-operation with sponsors, respectively	Revised. Duty of care of sponsors is numbered as Rule 10.4. Co-operation with sponsors is numbered as Rule 10.5 and the word "Undertaking" is replaced with "Person issuing the Securities". In new Rule 10.5(1), the word "Undertaking" is replaced with "Persons who make or intend to make a Prospectus Offer". The word "Undertaking" is replaced with "Offeror and Issuer" in Rule 10.5.(2) in relation to the sponsor's duty to notify the DFSA about non-co-operation
New Chapter 11	Compliance Advisers	Added new provisions re: Direction by DFSA to appoint compliance advisers for Reporting Entities
New Rule 11.1	Application of Chapter 11	
New Rule 11.2	Appointment of compliance adviser	
New Rule 11.3	Obligations of a Reporting Entity relating to a compliance adviser	
New Rule 11.4	Co-operation with compliance advisers	
New Rule 11.5	Termination of compliance adviser	Right of appeal to RAC re: direction to appoint compliance adviser
New Rule 11.6	Appeal to the Regulatory Appeals Committee (RAC)	