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**CONSULTATION PAPER NO. 70**

**25 APRIL 2010**

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**PROPOSED CHANGES TO ENFORCEMENT FRAMEWORK**

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## CONSULTATION PAPER NO 70

### PROPOSED CHANGES TO ENFORCEMENT FRAMEWORK

#### Why are we issuing this paper?

1. This Consultation Paper seeks public comments on the DFSA proposal to make changes to certain laws and Rules with respect to the DFSA enforcement framework. The proposed changes are designed to enhance the current framework to ensure the DFSA is able to regulate in an effective and efficient manner, and to reflect the DFSA's risk based approach to regulation.

#### Where can the changes be found?

2. This Consultation Paper details proposed changes to the following:
  - (a) Regulatory Law 2004; and
  - (b) Enforcement Module (ENF).

#### Who should read this paper?

3. The proposals in this paper would be of interest to Persons:
  - (a) Carrying on, or considering carrying on, any Financial Services, Ancillary Services or audits of Authorised Firms and Authorised Market Institutions; and
  - (b) Legal practitioners advising clients on enforcement related matters with respect to the DFSA.

#### How is this paper structured?

4. In this paper, we set out:
  - (a) the background to the proposals and overview (paragraphs 8 - 9);
  - (b) the proposed changes to the Regulatory Law 2004 and the Enforcement Module (paragraphs 10-34);

#### 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 the proposals is **25 May 2010**. 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 Regulatory Law 2004 and DFSA's Rulebook. You should not act on these proposals until the relevant changes to the Regulatory Law and DFSA Rulebook are made. We will issue a notice on our website telling you when this happens.

### **Comments to be addressed to:**

**Emmanuel Givanakis  
Senior Legal Counsel  
DFSA  
PO Box 75850  
Dubai, UAE**

**+971(0)4 3621533**

**or**

**e-mailed to: [egivanakis@dfsa.ae](mailto:egivanakis@dfsa.ae)**

## **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.

## **Background**

8. The Regulatory Law 2004 and the Enforcement Module of the DFSA Rulebook were enacted in September 2004. As part of the DFSA's ongoing review of the regulatory framework within the DIFC, we have reviewed the enforcement framework within which the DFSA operates.
9. As part of the review, consideration was given to recent enforcement and supervision activities undertaken by the DFSA. This was done in order to improve the effectiveness of the DFSA's enforcement capability and to better align enforcement related Laws and Rules with the DFSA's risk based approach to regulation.

## **Proposed changes**

10. The key changes proposed are as follows:
  - (a) increasing the amount that a Person may be fined, under the Regulatory Law 2004;
  - (b) widening the scope of contraventions and breaches for which an administrative fine or censure can be imposed; and
  - (c) enabling the DFSA to commence proceeding in the DIFC Court or before the Financial Markets Tribunal following a Notice of Objection to a fine for a contravention of the law or breach of the Rules.

### **A. Increasing the amount a Person may be fined**

11. The Regulatory Law 2004 provides the DFSA with the power to impose administrative fines. These fines are intended to be imposed in circumstances where the conduct involved in a contravention of the Laws or Rules administered by the DFSA is considered less serious in nature. These administrative powers are exercised within the parameters of ensuring the affected party is accorded procedural fairness and natural justice.
12. There have been no amendments to the quantum of fines since the law was enacted in September 2004. Currently, pursuant to Article 90(2) of the Regulatory Law 2004 the maximum amount that can be imposed is limited to US \$5,000 for a natural person and US \$25,000 for a body corporate.

13. In considering any increases to the amount that the DFSA can fine a Person we have reviewed several international jurisdictions and have ascertained that, by and large, financial services regulators internationally have considerable scope with respect to the amount that they can fine a Person (see **Appendix 3**). The benchmarking revealed the following:
- (a) The UK Financial Services Authority (UKFSA) and the US Office of the Comptroller of the Currency (OCC) have the ability to impose financial penalties for various amounts and for a broad range of contraventions and the amount is generally proportional to the regulator's view of the seriousness of the conduct that leads to these contraventions. Both regulators undertake an analysis of the particular factors and circumstances surrounding each matter in determining the seriousness of the conduct that led to the contravention and the appropriate amount of the fine. The factors and circumstances considered are contained in their respective policies and procedures manuals and include, for example, the gain or benefit to the offending party, any concealment of the contravention, the impact on other persons and the level of co-operation with the regulator.
  - (b) The Hong Kong Securities and Futures Commission (SFC) may impose fines of up to US\$1.3 million or three times the amount of the profit gained or loss avoided regardless of the seriousness of the conduct. These fines can be imposed for market misconduct and/or where the regulated person is found not to be fit and proper.
  - (c) The Monetary Authority of Singapore (MAS) can fine for a broad range of contraventions. The maximum amount that can be imposed administratively is dependant on the contravention, with maximums ranging from US\$8,900 to US\$36,000. However, the MAS is only able to impose these fines by way of a settlement, otherwise it must commence proceedings in the court.
  - (d) The Australian Securities and Investments Commission (ASIC), due to constitutional constraints, is only empowered to impose small fines for breaches of minor contraventions, for example, the failure to lodge an annual return. However, recently there have been efforts by the Australian Federal authorities to expand ASIC's powers to some degree with respect to market misconduct.
  - (e) The US Securities and Exchange Commission (SEC) after a hearing by an Administrative Law Judge, has the power to impose a civil penalty on a person on a broad range of contraventions. The amount of the penalty can range from US\$5,000 to US\$100,000 for an individual and US\$50,000 to US\$500,000 for a company depending on the seriousness of the conduct.
  - (f) The Ontario Securities Commission (OSC) after a hearing by a tribunal of the Commission, has the power to impose fines for a wide variety of offences where it is in the public interest to do so. The maximum amount that can be imposed is US\$984,000. The amount imposed depends on the seriousness of the conduct.
  - (g) Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) has a broad range of administrative fining powers with respect to the various

legislative responsibilities it has in banking, insurance and securities. BaFin can impose administrative fines in relation to breaches of the legislation it administers that are designated as an 'Administrative Offence'. The amounts that can be imposed vary from US\$67,000 to US\$1.35 million, depending on the seriousness of the contravention as prescribed in the legislation and the conduct that led to the breach.

14. Furthermore, in light of the DFSA's proposal to expand the scope of administrative fines (as discussed further in section B below), the DFSA will have the flexibility to impose fines in relation to a much greater variety of conduct that is less serious in nature. The DFSA will consider a number of factors and circumstances before it imposes an administrative fine.
15. The DFSA considers that the seriousness of the conduct involved in a contravention can vary, depending on the particular facts and circumstances. Isolated, one-off, or unintended breaches would generally be considered as being less serious whilst repeated, systemic and intentional breaches would be considered as being more severe and aggravated in nature. When determining whether to impose an administrative fine and the quantum of such a fine the DFSA will take into account a number of circumstances and factors, including, for example, whether the conduct was deliberate or reckless and whether the contravention is continuing.
16. Where the circumstances and factors in a matter are of a more serious nature the DFSA would not consider proceeding by way of administrative fine. Instead the DFSA would consider commencing proceedings in either the Financial Markets Tribunal or the DIFC Court, unless the matter is settled by way of Enforceable Undertaking.
17. In light of our review and the need to provide an appropriate and credible deterrent for less serious conduct, we propose to increase the amounts available to the DFSA with respect to administrative fines. The maximum amounts proposed are US\$20,000 for a natural person and US\$100,000 for a body corporate.
18. The DFSA is mindful of its duty to use its powers in a manner proportionate to its regulatory objectives and will be cognisant of this when imposing administrative fines. Furthermore, from a policy perspective, the DFSA would not generally seek to impose more than one administrative fine in relation to multiple contraventions which are closely connected to the same set of facts and circumstances. This is because to do so could raise the level of financial penalty disproportionately in relation to less serious conduct.
19. The DFSA does not propose to reduce any of the safeguards that a person currently has pursuant to the Rules. The current process for administrative fines does not necessitate an appeal by the Person. This is due to the Person having the right to file a Notice of Objection with the DFSA, which has the effect of ending the administrative process. As a result, the filing of a Notice of Objection places the onus on the DFSA to commence proceedings afresh in the Financial Markets Tribunal, or to take note of the objections and not pursue the matter further.
20. The proposed amendments are contained in **Appendix 1 and Appendix 2**

## **B. Widening the scope of Administrative Fines and Censures**

21. The range of contraventions for which the DFSA may impose administrative fines and censures is limited by ENF Rules 7.12.1 and 7.13.1. The benchmarked jurisdictions referred to earlier in this paper generally do not limit, to the same extent, the contraventions against which administrative fines may be imposed. For example, the UKFSA has the ability to impose administrative fines or censures for any misconduct, which is broadly defined, covering the full scope of the UKFSA Handbook Rules, including the principles that apply to authorised firms and approved persons.
22. The DFSA considers that it should have the power to impose administrative fines and censures in relation to a wide variety of contraventions where the conduct is of a less serious nature. This is particularly so where a negotiated outcome cannot be reached. However, the DFSA acknowledges that there are limits with respect to the subjective view of seriousness, and is mindful of this when determining whether to impose an administrative fine. An administrative fine or censure can be a proportionate, efficient and effective way of concluding a matter rather than commencing proceedings in the Financial Markets Tribunal or DIFC Court.
23. Where the conduct with respect to any contravention is serious, however, the DFSA would not rely on administrative fining and censoring powers under Rule 7.12 and 7.13, but would pursue the matter before the Financial Markets Tribunal or the DIFC Court, unless the matter was settled by way of an Enforceable Undertaking.
24. The DFSA intends to retain the status quo in relation to contraventions of Article 30 and 35 of the Regulatory Law 2004. Accordingly, these contraventions cannot attract an administrative fine or censure. Article 30 relates to the Regulatory Appeals Committee (RAC) regarding situations where a person contravenes, for example, an order, prohibition or requirement of the RAC. Article 35 relates to the Financial Markets Tribunal and refers to situations where a person contravenes, for example, an order, notice, prohibition or requirement of the Financial Markets Tribunal.
25. The proposed amendments are contained in **Appendix 2 (ENF Module)**.

## **C Commencement of Proceedings in the DIFC Court**

26. Where a Notice of Objection is filed by a person upon whom an administrative fine has been imposed, the Rules in Chapter 7 of the Enforcement Module enable the DFSA to commence proceedings only in the Financial Markets Tribunal, or to take note of the objections and decline to pursue the matter.
27. We believe the Rules and Guidance should be amended to add to the options available to the DFSA that it be able to commence proceedings in the DIFC Court.
28. The rationale for this inclusion is that the Financial Markets Tribunal does not sit permanently and does not have the DIFC Court's range of interlocutory powers. In particular the Financial Markets Tribunal's power to make interlocutory orders is limited to procedural matters. The DFSA may need to take urgent

interlocutory action where there are ongoing contraventions of the Law or Rules, after a Notice of Objection has been filed by the Person.

29. Similarly, in relation to administrative censures, the Enforcement Module under Rules 7.13.3, 7.13.4 and 7.13.5, only refers to commencing proceedings in the Financial Markets Tribunal. The DFSA believes these Rules and Guidance should be amended to allow the DFSA to also be able to commence proceedings in the DIFC Court.
30. In the event that a written notice regarding an administrative censure or fine is objected to, and the DFSA wishes to pursue the matter, the DFSA believes that it should not be limited in the range of *fora* available to it.
31. The proposed amendments are contained in **Appendix 2** (ENF Module)

#### **D Information Gathering and Investigation Powers**

32. It is proposed that Guidance under section 5.1 of the Enforcement Module be amended by deleting *"In general, the DFSA will use only those powers that allow it to achieve its objectives whilst causing the least possible interference with the activities of the participants in the DIFC."*
33. It is the DFSA's view that, although this is reflective of its general approach, it may fetter its broad discretion when exercising its regulatory powers to achieve its objectives. The general tenor of the statement is already encapsulated in the overriding guiding principles of the DFSA, found under Article 8(4) of the Regulatory Law of 2004.
34. The proposed amendments are contained in **Appendix 2 (ENF Module)**.