



CONSULTATION PAPER NO. 81

12 DECEMBER 2011

**THE EXERCISE OF REGULATORY POWERS,
ENHANCEMENTS TO THE REGULATORY LAW 2004 AND RPP
SOURCEBOOK**

CONSULTATION PAPER NO 81

THE EXERCISE OF REGULATORY POWERS, ENHANCEMENTS TO THE REGULATORY LAW 2004 AND RPP SOURCEBOOK

Why are we issuing this paper?

1. This Consultation Paper presents enhancements to the Regulatory Law 2004 and additional chapters to the Regulatory Policy and Process (RPP) module of DFSA's Sourcebook. These chapters outline the DFSA's policies and processes when exercising its supervisory and enforcement powers, and the type of decision making procedures it will adopt when exercising such powers.
2. There is no obligation on the DFSA to consult on the proposed release of the additional chapters of the RPP module. However, the DFSA has included the proposed RPP chapters for information purposes. Accordingly, this paper seeks public comment on the DFSA's proposal to:
 - (a) change its requirements relating to the imposition of administrative fines and censures; and
 - (b) consolidate its enforcement powers in the Regulatory Law 2004.

Who should read this paper?

3. The proposals in this paper would be of interest to:
 - (a) Persons carrying on, or considering carrying on, Financial Services in or from the DIFC;
 - (b) Persons carrying on or considering carrying on, Ancillary Services in or from the DIFC,
 - (c) Registered Auditors, or auditors considering becoming a Registered Auditor;
 - (d) Authorised Individuals; and
 - (e) advisors to those Persons.

How is this paper structured?

4. In this paper we set out:
 - (a) the background to the RPP module (paragraphs 8 to 13);
 - (b) our proposal to add three new chapters to the RPP module (paragraphs 14 to 22);

- (c) our proposal to change the process for imposing administrative fines and censures (paragraphs 23 to 35);
- (d) our proposal to repeal the Enforcement module and recommend to the Ruler to make changes to the Regulatory Law 2004 (paragraphs 36 to 38); and
- (e) other miscellaneous changes (paragraphs 39 to 43).

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. 81
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 **21 January 2012**. Once we receive your comments, we shall consider if any further refinements are required to these proposals. We shall then proceed to recommend the proposed changes to the Regulatory Law 2004 to the President for enactment by the Ruler. If the proposed changes to the Regulatory Law 2004 are enacted, we shall then proceed to enact the relevant changes to the DFSA's Rulebook. You should not act on these proposals until the relevant changes to the Regulatory Law 2004 and DFSA Rulebook are made. We shall issue a notice on our website telling you when this happens.

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.

The Regulatory Policy and Process module

8. On 28 April 2011, a new module of DFSA's Sourcebook known as the Regulatory Policy and Process module (RPP) came into force. The RPP Sourcebook was created to contain information such as:
 - (a) statements of DFSA's regulatory policy;
 - (b) descriptions of the regulatory processes that we follow when exercising our statutory powers;
 - (c) information as to DFSA's risk based approach to authorisation, supervision and enforcement; and
 - (d) information on matters which the DFSA may assess when considering whether to exercise discretionary powers. For example, this would include those matters which the DFSA may take into consideration when making an assessment of whether an Authorised Person or Authorised Individual is fit and proper.
9. In removing the process and procedural notes currently in the form of Guidance from several modules of DFSA's Rulebook, the RPP module was created with the following initial chapters:
 - (a) Chapter 1 – Introduction;
 - (b) Chapter 2 – Authorisation – Becoming Regulated; and
 - (c) Chapter 3 – Supervision – Being Regulated.
10. Subject to the consequential changes to the Regulatory Law 2004 discussed below being enacted by the Ruler, the DFSA proposes to release the following new chapters to the RPP module:
 - (a) Chapter 4 – Supervisory and Enforcement Powers;
 - (b) Chapter 5 – Enforcement; and
 - (c) Chapter 6 – Decision Making.
11. In creating these new chapters of the RPP module, the DFSA is relocating its existing enforcement policies and process information currently located in the ENF module of its Rulebook. The DFSA has also taken the opportunity to review and update these policies and processes.

Associated changes to the ENF Module and the Regulatory Law 2004

12. The removal of the policy and process information from the ENF module to the RPP module has resulted in only a few Rules remaining in the ENF module. Therefore, the DFSA is proposing to recommend to the Ruler to transfer and incorporate the remaining ENF Rules with their substantive powers into the Regulatory Law 2004. Consequently, the DFSA will no longer have an ENF module as part of its Rulebook.
13. There is no obligation on the DFSA under the Regulatory Law 2004 to consult on the proposed release of the additional chapters of the RPP module. The consequential changes to the ENF module and the proposed recommendations to the Ruler to change the Regulatory Law 2004 do, and so the DFSA has decided to include in this paper for information purposes, the changes to the RPP module.

Chapter 4 – Supervisory and Enforcement Powers

14. Chapter 4 of the RPP module (see Appendix 1) discusses the key powers which the DFSA uses when conducting either supervisory or enforcement action (with Chapter 5 of RPP dealing with the remaining key powers used when the DFSA is conducting enforcement action).
15. Some of the key powers described in chapter 4 include the power to:
 - (a) request information and documents and access premises;
 - (b) require an Authorised Person to provide a report from an Independent Expert;
 - (c) impose restrictions on an Authorised Person's business or dealings with relevant property;
 - (d) impose conditions and restrictions on an Authorised Person's Licence;
 - (e) withdraw the authorisation under an Authorised Person's Licence to conduct one or more specified Financial Services;
 - (f) withdraw the Licence of an Authorised Person;
 - (g) impose conditions and restrictions on an Authorised Individual's status;
 - (h) restrict, suspend or withdraw an Authorised Individual's status; and
 - (i) suspend, vary or withdraw the registration of an Ancillary Service Provider or Registered Auditor.

Chapter 5 – Enforcement

16. Chapter 5 of the RPP module (see Appendix 2) discusses the DFSA's approach to enforcement, how it commences and conducts investigations, and how it exercises its powers to address misconduct or contraventions of Laws or Rules.
17. The DFSA's key enforcement powers, policies and processes described in this chapter include the following;
 - (a) the process for the assessment of complaints and referrals;

- (b) the process for commencing an investigation and the role of the Enforcement Committee;
- (c) the powers to gather information and documents;
- (d) the powers to fine or censure a Person;
- (e) the powers to commence proceedings before the Financial Markets Tribunal or the Court; and
- (f) the policies in relation to determining financial penalties, entering into settlement discussions and accepting an Enforceable Undertaking.

Chapter 6 – Decision Making

- 18. Chapter 6 of the RPP module (see Appendix 3) sets out the decision making procedures which the DFSA will generally follow when exercising its powers. This chapter builds upon information previously in appendix 3 of the ENF module. Decisions generally fall into two categories, referred to as either an Executive Decision or a Decision Maker decision.
- 19. Executive decisions are operational decisions made on a day to day basis by the DFSA. These decisions will mainly involve the DFSA being called upon to make a decision in response to an application or notification given by a Person to the DFSA. An example of such a decision is where the DFSA approves an application for a change in control by an Authorised Person.
- 20. The DFSA will follow its decision maker procedures when it exercises particular supervisory and enforcement powers which affect the rights of Authorised Persons, such as its power to withdraw a Licence. In such circumstances, a DFSA Officer (known as a Decision Maker), will be appointed to determine whether the DFSA should exercise its powers.
- 21. To assist the regulated community, chapter 6 of the RPP contains an appendix which sets out the DFSA's various powers and the decision making procedures it will generally follow prior to exercising such powers.
- 22. There are three associated consultation papers to take into account when considering any relevant Laws and Rules referred to in the appendix to chapter 6. These papers are:
 - (a) Consultation Paper 75 (Proposed Changes to the Markets Law Regime), where the DFSA consulted upon proposed changes to the Markets Law and creation of the Markets Rules (MKT) module. The consultation period ended on 18 July 2011 and after due consideration of consultees comments, the final version of the changes, subject to approval by the Ruler, will be included in the relevant Laws and Rules;
 - (b) Consultation Paper 76 (Proposed Changes to the Markets Law Regime Part 2 - Recognition and Auditing), where the DFSA consulted upon proposed changes to expand its supervisory oversight of auditors to include audit firms for DIFC incorporated companies that are listed on an Authorised Market Institution. The consultation period ended on 4 August 2011 and after due consideration of consultees comments, the final version of the changes, subject to approval by the Ruler, will be included in the relevant Laws and Rules; and

-
- (c) Consultation Paper 80 (Proposals relating to Controllers of Authorised Persons), where the DFSA is consulting upon proposals to enable the DFSA to ensure that Controllers do not have any adverse impact on an Authorised Person's fitness and propriety or their ability to conduct business in a prudent and sound manner. The consultation period ended on 8 December 2011 and after due consideration of consultees comments, the final version of the changes, subject to approval by the Ruler, will be included in the relevant Laws and Rules.

Changes to administrative fines and censures

- 23. The DFSA previously reviewed its fining and censure powers as part of the changes proposed through Consultation Paper No. 70 – Proposed Changes to the Enforcement Framework. These changes resulted in the DFSA:
 - (a) increasing the quantum of its administrative fines (i.e. up to the maximum of \$20,000 in respect of a natural person and \$100,000 in respect of a body corporate);
 - (b) widening the range of contraventions for which it could impose an administrative fine and censure; and
 - (c) obtaining the ability to commence proceedings in either the Financial Markets Tribunal (FMT) or the Court where a Notice of Objection is filed in relation to a fine or censure.
- 24. The DFSA's experience with imposing administrative fines and censures has led it to consider that its process for exercising such powers can be simplified and improved.
- 25. The DFSA has the power to issue an administrative fine pursuant to Article 90 of the Regulatory Law 2004 and section 7.12 of the ENF module. The DFSA also has the power to issue an administrative censure pursuant to Article 91 of the Regulatory Law 2004 and section 7.13 of the ENF module.
- 26. The DFSA will generally seek to impose an administrative fine in respect of less serious conduct or contraventions. Where, however, the circumstances and factors in a matter are of a more serious nature, the DFSA would consider commencing proceedings in either the Financial Markets Tribunal (FMT) or the Court.
- 27. The current process for an administrative fine and censure is as follows:
 - (a) the DFSA will generally consider exercising such powers after conducting an investigation;
 - (b) an internal committee of the DFSA (the Enforcement Committee) will consider the outcome of any investigation and make a decision as to whether to issue a Notice of Administrative Fine or Notice of Administrative Censure as applicable;
 - (c) in respect of a Notice of Administrative Fine, the recipient of such notice has one of three options:
 - (i) agree to pay the fine;
 - (ii) object to the fine by filing a Notice of Objection; or

- (iii) do nothing.

 - (d) If the recipient of a Notice of Administrative Fine objects to the fine, the onus is on the DFSA to commence proceedings afresh in the FMT or the Court. If the recipient does not object, or does not pay the fine after the conclusion of the period specified in the notice, the DFSA may recover the fine as a debt due, together with costs;

 - (e) in respect of a Notice of Administrative Censure, the recipient of such notice has one of four options:
 - (i) agree to the censure;
 - (ii) make representations in relation to the imposition of the censure;
 - (iii) object to the censure by filing a Notice of Objection; or
 - (iv) do nothing.

 - (f) if the recipient of a Notice of Administrative Censure elects to make representations, the DFSA will appoint a Decision Maker to consider such representations. If the recipient wishes to object to the censure, the onus is on the DFSA to commence proceedings afresh in FMT or the Court. If the recipient does nothing, after the period specified in the notice, the DFSA may proceed to censure the person in the manner set out in the notice.
26. The DFSA currently appoints a Decision Maker to consider whether it should exercise its powers to withdraw an authorisation or Licence of an Authorised Person. The DFSA's process to appoint a Decision Maker is currently set out as guidance in the ENF module (see guidance point 18 to section 2.2 and appendix 3.1 of the ENF Module).
27. The DFSA proposes to also opt for a Decision Maker model in respect of its administrative powers to fine and censure. This is supported by the benchmarking discussed below.
28. In reviewing its administrative fine and censure processes, the DFSA conducted benchmarking of other financial services regulators such as the:
- (a) UK Financial Services Authority (UK FSA);
 - (b) US Securities Exchange Commission (SEC);
 - (c) US Office of the Comptroller of the Currency (OCC);
 - (d) Hong Kong Securities and Futures Commission (SFC);
 - (e) Ontario Securities Commission (OSC);
 - (f) German Bundesantalt fur Finanzdienstleistungsaufsicht (BaFin); and
 - (g) Australian Securities and Investments Commission (ASIC).

-
29. Generally, the benchmarking supports regulators having administrative powers to fine and censure and highlights two models, which can be described as follows:
 - (a) "Decision Maker" model where an individual has the authority to impose a fine or censure on a Person (SEC, OCC and SFC, and to a limited extent, BaFin and ASIC); and
 - (b) "Committee" model where a statutory committee has the authority to impose a fine or censure on a Person (UK FSA and OSC).
 30. Therefore, the DFSA proposes to change its process for deciding on whether to impose an administrative fine or censure. The new process will involve the Enforcement Committee appointing a Decision Maker and for that Decision Maker to:
 - (a) give a Person a suitable opportunity to make representations prior to deciding whether he should fine or censure such person; and
 - (b) provide reasons for any decision to exercise such power.
 31. The DFSA proposes to recommend to the Ruler to provide an affected Person with the right to appeal the decision of a Decision Maker to the Regulatory Appeals Committee. The Decision Maker will inform the Person of his right of appeal to such committee. A Person may further appeal the decision of the Regulatory Appeals Committee by way of judicial review proceedings before the Court on a point of law.
 32. The DFSA has also reviewed the purpose behind ENF Rules 7.12.3 and 7.13.8. These Rules provide that no proceedings may be commenced by the DFSA in respect of a relevant contravention, where the Person has paid the fine within the specified period or agreed to a censure.
 33. The DFSA considers those Rules could be viewed as ambiguous and may arguably prevent the DFSA from taking other action including, for example, protective action (such as placing a restriction on an Authorised Individual's status) in respect of a contravention for which a Person has paid a fine or agreed to a censure. Such a restriction might prevent the DFSA from meeting its objectives in certain circumstances.
 34. Therefore, in order to ensure greater clarity, the DFSA proposes to remove ENF Rules 7.12.3 and 7.13.8
 35. In regard to pursuing other remedies, the DFSA notes it will not seek a fine from the FMT, where an administrative fine has already been imposed and paid in relation to the same contravention (see Article 87(1) of Regulatory Law 2004). Furthermore, the DFSA will act fairly, openly, accountably and proportionally when exercising its powers in accordance with its statutory objectives.

Issues for consideration

1. Do you have any concerns or comments about our proposed changes to our procedures relating to the imposition of an administrative fine and censure?

Changes to the Enforcement Module and the Regulatory Law 2004

36. The relocation of the enforcement and decision making information to the RPP, leaves a handful of Rules in the ENF module. Therefore, we propose to recommend to the Ruler that the remaining ENF rules be added to the Regulatory Law 2004. A few of these Rules either clarify or expand upon existing powers set out in the Regulatory Law 2004. Given the changes proposed to administrative fines and censures, the DFSA has taken the opportunity to recommend to the Ruler to consolidate and relocate the remaining ENF Rules with their substantive powers (articles 80, 88, 90 and 91) in the Regulatory Law 2004 (see Appendix 4). The DFSA notes that other Financial Services regulators have their enforcement powers located in their primary legislation.
37. The proposed chapters 4, 5 and 6 of the RPP module and recommended changes to the Regulatory Law 2004, would result in the DFSA no longer having an ENF module in its Rulebook.
38. To help readers follow the proposed changes resulting from the DFSA no longer having an ENF module, we have prepared a destination table which is attached to this Consultation Paper (see Appendix 5).

Issues for consideration

2. Do you have any concerns or comments about our proposed re-structuring of the enforcement powers?

Miscellaneous changes

39. In reviewing the existing Rules in the ENF module, the DFSA has reviewed its requirements relating to certain circumstances the DFSA may consider in deciding to withdraw an Authorised Individual's status.
40. Article 58(3)(b) of the Regulatory Law 2004 provides the DFSA with discretion to withdraw the status of an Authorised Individual, where such person is convicted of a "serious criminal offence." It is important to note that by virtue of Article 59(2), the DFSA may make such a decision, without giving such a person a suitable opportunity to make representations.
41. Pursuant to ENF Rule 7.8.1, the DFSA may determine that a Person has been convicted of a serious offence, if that Person has been convicted of any offence in respect of which the maximum penalty includes imprisonment.
42. The benchmarking conducted by the DFSA highlighted that ASIC has a similar power to Article 58(3)(b) and has limited such power to offences involving serious fraud. Whilst the UK FSA and Hong Kong's SFC do not have an equivalent power to Article 58(3)(b), both regulators give particular attention to offences relating to dishonesty, fraud and financial crime in assessing the fitness and propriety of their licensed individuals.
43. Accordingly, in line with its benchmarking, the DFSA proposes to remove ENF Rule 7.8.1 and replace it with guidance in the RPP outlining how the DFSA will give particular consideration to offences involving dishonesty, fraud or a financial crime, when considering whether a Person has been convicted of a serious criminal offence under Article 58(3)(b).

Issues for consideration

3. Do you have any concerns or comments about our proposed changes to the type of serious criminal offences the DFSA may consider under Article 58(3)(b) of the Regulatory Law 2004?

Other matters

44. It is proposed that the changes to the ENF module will come into effect at the same time as the changes proposed to the Ruler in respect of the Regulatory Law 2004.
45. The DFSA will keep the regulated community updated on progress and provide sufficient time for changes to relevant policies, procedures, systems and controls and other matters prior to the coming into force of the relevant Laws, Rules and the RPP module.
46. Finally, we recognise that the proposed changes to the processes of an administrative fine and censure will impact on any ongoing proceedings in respect of a Notice of Administrative Fine or Notice of Administrative Censure issued by the DFSA prior to the coming into force of the proposed changes, which have not been finalised.
47. We have therefore included transitional rules in GEN Chapter 10 (see Appendix 6) which will enable any ongoing proceedings in respect of an administrative fine and censure to be dealt with in accordance with the existing requirements in Articles 90 and 91 of the Regulatory Law 2004 and the ENF module.