CONSULTATION PAPER NO. 106

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REGULATION OF ARRANGING, REPRESENTATIVE OFFICE ACTIVITIES AND FINANCIAL PROMOTIONS

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Part A: Introduction and Overview

Why are we issuing this paper?

1. The Dubai Financial Services Authority (the DFSA) proposes to enhance the regulation of Persons:

   (a) carrying on the Financial Services of 'arranging':[1]

   (b) operating Representative Offices (Rep Office); [2] and

   (c) undertaking Financial Promotions in or from the DIFC.[3]

   Peripherally, these proposals also deal with the Financial Services of 'Advising on financial products and credit'[4] and 'Providing Custody'.[5] We propose some changes in these two areas only so far as are needed to give full effect to the proposed changes referred to in (a) above.

2. We became aware, during our supervision process, that there are some unintended gaps and overlaps in regulation. These seem to have arisen due to a combination of factors:

   (a) Arranging activities (e.g. arranging to enable other people to transact or obtain financial services) sit on the same spectrum of activities as 'referrals' and 'financial promotions'. The latter attracts less onerous regulation than 'arranging' activities. This apparently gives an incentive for persons carrying on referrals and financial promotions to 'trespass' into 'arranging' activities, resulting in regulatory arbitrage.

   (b) A lack of clarity in some areas of regulation, which increases scope for entities to trespass into areas which they are not regulated for, as noted above.

   (c) A lack of clarity between 'arranging' activities and the substantial Financial Services which are arranged for – again providing scope for unintended

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1 There are six types of Financial Services that comprise 'arranging' activities. These are, 'Arranging credit or deals in Investments' (GEN Rule 2.9.1), 'Arranging Long-Term Insurance' (GEN Rule 2.9.1), 'Insurance Intermediation' (GEN Rule 2.19.1), 'Insurance Management' (GEN rule 2.20.1), 'Arranging Custody' (see GEN Rule 2.14.1) and 'Providing Trust Services (GEN Rule 2.23.1(b)).

2 See GEN Rule 2.26.1.

3 See GEN chapter 3.

4 See GEN Rule 2.11.1.

5 See GEN Rule 2.13.1.

contraventions of the boundaries of the relevant Financial Services. Examples are the boundary between 'Arranging Custody' and 'Providing Custody' and similarly, the boundary between 'Arranging Deals in Investments' and 'Dealing in Investments as Agent'.

Overview of the proposals

3. Our proposals are designed to provide greater clarity, certainty and flexibility to those undertaking intermediation activities in the DIFC, and to provide a regulatory framework which is proportionate to the risks associated with their activities. These proposals build upon the recent changes to the insurance regime resulting from Consultation Paper 103 (CP103), which come into force on 1 August 2016.

4. In this paper, we propose, among other things, to:

   (a) retain the current overall form and level of regulation of 'arranging' and 'advising' activities;

   (b) make some refinements to provide greater clarity and regulation along functional lines for the relevant financial services (for example, amalgamating arranging and advising activities relating to credit as a separate Financial Service, as opposed to keeping them as part of 'Investment-related' Financial Services);

   (c) introduce changes to ensure 'arranging' and 'advising', as well as 'acting as agent', activities relating to Long-Term Insurance are regulated in a manner consistent with the regulation of similar activities relating to other contracts of insurance; and

   (d) introduce more comprehensive Guidance relating to 'arranging' and 'advising' activities vis-a-vis the relevant financial products or Financial Services to which arranging relates, to provide greater clarity relating to the distinction between such activities;

   (e) remove significant ambiguities relating to the restrictions that apply to Rep Offices by:

      (i) specifying in the definition itself the limitation that a Rep Office can only market financial products and financial services of its related parties located outside the DIFC;

      (ii) specifying that a Rep Office can only approve financial promotions if such promotions relate to financial products and financial services of its related parties located outside the DIFC;

      (iii) clarifying that Rep Offices are not permitted to hold monies belonging to its head office clients; and

      (iv) giving extensive Guidance to address issues which have already been raised through supervision activities – particularly to promote better understanding of the Rep Office regime by Rep Office employees;

   (f) address unintended gaps and effects, such as removing the application of Client

Asset provisions to firms 'Arranging Custody'; and

(g) refine the Financial Promotions regime to minimise the risk of abuse of that regime.

5. We also propose, as an incidental part of providing clarity in the areas reviewed, a few changes in other related areas. For example, to provide clarity on how 'arranging' activities can be distinguished from the substantive Financial Service or financial product to which that activity relates, such as the distinction between:

(a) 'Arranging Deals in Investments' and 'Dealing in Investments as Agent'; and

(b) 'Arranging Custody' and 'Providing Custody'.

Who should read this paper?

6. The proposals in this paper would be of interest to Persons carrying on or proposing to carry on:

(a) Arranging credit or deals in Investments;

(b) Advising on financial products and credit;

(c) Insurance Intermediation;

(d) Insurance Management;

(e) Arranging Custody;

(f) Providing Custody;

(g) Providing Trust Services;

(h) Operating Representative Offices and their head offices;

(i) Financial Promotions in or from the DIFC;

(j) the role of industry bodies; and

(k) the role of being users or participants in the services offered by Persons referred to above.

Terminology in this paper

7. In the remainder of this paper, 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) of the DFSA Rulebook. Unless the context otherwise requires, where capitalisation of the initial letter is not used, the expression has its natural meaning. All references to Rules in Appendices 2 – 6 are references to proposed Rules.

How to provide comments?

8. All comments should be sent to the email specified below. Please use the Consultation Paper number in the subject line. Please also use the Table at Appendix 7 to provide your comments. 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 emailed to consultation@dfsa.ae

What happens next?

9. The deadline for providing comments on this consultation is 21 August 2016. Once we receive your comments, we will consider if any further refinements are needed to these proposals. We will then proceed to make the relevant 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.

Structure of this paper

10. The proposals in this paper are structured as follows:

(a)	Part A:	Introduction and Overview;
(b)	Part B:	Background;
(c)	Part C:	Proposals relating to the overall structure for regulating arranging and advising activities;
(d)	Part D:	Proposals to promote greater clarity relating to the regulation of arranging and advising activities;
(e)	Part E:	Proposals relating to Representative Offices;
(f)	Part F:	Proposals relating to Financial Promotions;
(g)	Part G:	Transition; and
(h)	Part H:	Other aspects.
(i)	Appendix 1:	Benchmarking;
(j)	Appendices 2–6:	Draft amendments to the GEN, COB, REP, GLO, and PIB Modules; and
(k)	Appendix 7:	Table for providing comments.

Part B: Background

11. As noted in paragraph 2, we became aware, through our supervisory work, of ambiguities relating to the boundaries of those activities. We first addressed the threshold issue whether any of the activities subject to review pose sufficient regulatory risks to the users of such services, and the DIFC markets, to warrant regulation. We conclude that they merit regulation and, apart from the proposed refinements and additional Guidance to promote greater clarity, there is no strong case for removing regulation of these activities.

12. The proposals in this paper are designed to address the unintended gaps and overlaps identified to minimise opportunities for regulatory arbitrage and to provide greater certainty for Persons conducting those activities.

13. Our regime regulating arranging/advising activities as Financial Services largely follows, as a proxy for the EU regime, the UK regime. Our regime also takes into account DIFC specific factors, as well as practices in other comparable jurisdictions noted before, and international developments. We have remained aligned with the UK regime as many firms in the DIFC ('Centre') have their headquarters and home operations in the EU, although we note that this profile may be changing.

14. A key objective of the DFSA regime is to meet standards set by international standard setting bodies. Such observance is important because the International Monetary Fund and the World Bank, in their Financial Sector Assessment Programme ("FSAP"), assess regulatory regimes against the IOSCO, Basel and IAIS standards, as applicable.[6] Therefore, the proposals in this paper aim to maintain our continued compliance with these standards.

Overview of the current regime

<u>The regime for firms carrying on arranging and advising business</u>

15. Under the current regime, there are a number of Financial Services which cover 'arranging' and 'advising' activities. These are:

    (a) Arranging credit or deals in Investments;

    (b) Advising on financial products or credit;

    (c) Insurance Intermediation;

    (d) Insurance Management;

    (e) Arranging Custody; and

    (f) Providing Trust Services.

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[6] International standards are set by the Basel Committee of Banking Supervisors (BCBS) for the banking sector, the International Association of Insurance Supervisors (IAIS) for the insurance sector and the International Organization of Securities Commissions (IOSCO) for the securities sector.

16. Each of these incorporates different forms of intermediation activities that lead to other people entering into financial transactions. There are three main categories of intermediation activities:

    (a) 'advising' potential investors/customers about the merits of obtaining a financial product or credit;

    (b) 'arranging' for other people (e.g. buyers and sellers) to transact;[7] and

    (c) 'acting as agent' for a buyer or seller.

17. Our current definitions of Financial Services encompass the above intermediation activities in different ways depending on the type of financial instrument or financial sector.[8] Our definitions also cover different financial instruments and financial sectors.[9]

18. Firms conducting the above activities have to meet the requirements in GEN. These include having to be authorised to conduct the relevant Financial Service and meeting conduct requirements. To obtain and maintain a Licence, a firm must demonstrate, and thereafter meet on an on-going basis, the fitness and propriety, capital and systems and controls requirements in our Rulebook.

19. These firms attract the COB requirements relating to client classification, core rules applicable to all firms, and certain additional rules depending on whether they are conducting Investment Business, insurance activities, or Providing Trust Services.

    The Representative Office regime

20. A Rep Office is permitted under its Licence to 'market one or more financial services or financial products which are offered in a jurisdiction outside the DIFC'. A Rep Office can only market financial services and financial products offered outside the Centre by its own head office, and those of its Group members. These Firms are not subject to the prudential regime in PIB and the COB regime.

    The Financial Promotions regime

21. Authorised Firms can conduct Financial Promotions in or from the Centre and also approve financial promotions of other parties. Non-DIFC entities (i.e. Persons who do not have a place of business in the DIFC) can carry on Financial Promotions provided

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7 Arranging potential borrowers to obtain credit from a credit provider, arranging a potential investor to obtain custody services from a custody provider or arranging a person to act as trustee under a trust arrangement, are also arranging activities.

8 For example, all three intermediation activities of 'advising', 'arranging' and 'acting as agent' relating to Contracts of Insurance (other than LTI) fall within a single Financial Service of Insurance Intermediation. In contrast, Investment Business (which includes advising on, and arranging, LTI), has three Financial Services to cover the above activities, i.e. 'Advising on financial products', 'Arranging deals in Investments' and 'Dealing in Investments as agent'. With regard to intermediation activities relating to credit, only 'arranging' and 'advising on' credit are regulated as a Financial Service. With regard to 'custody', while 'arranging' custody is a Financial Service, both 'advising on' custody arrangements and 'acting as agent' for a custody provider are not regulated intermediation activities.

9 See the definitions of 'Arranging credit or deals in Investments' and 'Advising on financial products or credit'.

they do not do so by way of business, i.e. infrequently, and also subject to certain requirements, i.e. the Financial Promotion being approved by an Authorised Firm.

Part C: Proposals relating to the overall structure for regulating arranging and advising activities

22. We considered the following issues relating to the current structure of regulation of arranging and advising activities:

    (a) Should arranging activities relating to Investments, credit, and custody be regulated as Financial Services?

    (b) Should we continue to regulate 'Advising on credit' as a Financial Service?

    (c) How should the arranging and advising activities relating to Long-Term Insurance be regulated?

    (d) Should any changes be made to the activities excluded from regulation as arranging and advising?

(a) Should arranging activities relating to Investments, credit, and custody be regulated as Financial Services?

23. We considered whether the arranging activities, relating to deals in Investments, credit or custody, pose any regulatory risks that justify their regulation and whether doing so is consistent with the international standards and practices in similar jurisdictions.

Arranging Deals in Investments

24. The activity of arranging deals in Investments poses a number of risks. For example, the arranger may, for personal gain (e.g. commissions or fees paid to him by the provider of the financial service or product), induce a customer to obtain a financial service or product which is not needed or appropriate for the customer (i.e. mis-selling). If the arranger handles customers' money or Investments, without regulation of that activity, there will be no systems and controls to mitigate loss of such assets in the hands of the 'arranger'.[10] An Arranger's fitness and propriety (which includes integrity) will also not be subject to any scrutiny, allowing unscrupulous players to engage in such activities in an unacceptable manner.

25. To address the above risks, consistent with the practices in comparable jurisdictions benchmarked (See Appendix 1), we propose to continue regulating 'Arranging Deals in Investments' as a Financial Service (see draft GEN Rule 2.9.1 in Appendix 2).

Arranging Credit

26. A credit provider is more at risk than the borrower (customer), and therefore, would generally undertake due diligence regarding the repayment capabilities of the customer. This does not mean that the customer is also not at risk. Some of the mis-

[10] Under our current regime, while a firm which carries on 'arranging' activities is prohibited from holding client money, it can hold other client assets (i.e. Investments) subject to additional controls.

selling risks noted in paragraph 24 can arise, such as the arranger, for personal gain (e.g. commissions or fees paid to him by a lender), inducing a customer to obtain credit on inappropriate terms, or use collateral on unfavourable terms for the customer.

27. Although the DIFC regime does not permit firms to provide consumer credit to Retail Clients[11] (as in other benchmarked jurisdictions discussed below), we considered it appropriate to continue to regulate 'Arranging Credit' as a Financial Service because:

    (a) firms arranging (or advising on) credit are not prohibited from doing so for Retail Clients, including such clients borrowing for consumer and not for commercial purposes – provided the credit provider is in a jurisdiction outside the DIFC; and

    (b) there are risks associated with mis-selling, which can lead to reputational risks to the DIFC.

28. There is no functional similarity between Arranging Credit and Arranging deals in Investments, although both currently form part of a single Financial Service. The COB requirements are also different and more substantial for Investment-related activities than for credit-related activities. Therefore, we considered it appropriate to create two separate Financial Services for arranging activities relating to credit and deals in Investments (see draft GEN Rule 2.9.1 and GEN Rule 2.28.1 in Appendix 2).

Arranging Custody

29. This activity has raised many queries from industry participants, with regard to its scope and its interaction with the substantive Financial Service of 'Providing Custody'.

30. There is an overlap between the activities of a person 'Providing Custody' and a person 'Arranging Custody'. This is particularly the case where a firm 'Providing Custody' makes arrangements with third party service providers to hold custody of assets which the firm has agreed to safeguard for its Clients.

31. Under the current definition of 'Providing Custody', the activities of safeguarding and administering Investments belonging to another person constitute custody (along with providing custody in relation to Fund property and operating clearing houses).[12] 'Arranging Custody' is defined as arranging for one or more persons to conduct the activities defined as 'Providing Custody'.[13]

32. Our definitions of Providing Custody and Arranging Custody are derived from the UK definition of 'Safeguarding and administering Investments'. Under that definition, a person (A) is regarded as carrying on that activity if A safeguards and administers the assets belonging to another person (B), or arranges for a third party (C) to safeguard or administer the assets of B.[14]

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[11] See COB Rule 4.3.1(1), which provides that a firm may only Provide Credit to a Professional Client and if a Retail Client, if it is an Undertaking (e.g. a body corporate) which borrows for commercial purposes.

[12] See GEN Rule 2.13.1.

[13] See GEN Rule 2.14.1.

[14] The assets in relation to which safeguarding and administration is provided must include Securities or contractually based Investments. Securities can be held in dematerialised (i.e. uncertificated) form.

33. While our regime has two Financial Services (i.e. 'Providing Custody' and 'Arranging Custody'), essentially, what is covered by these two Financial Services are the same as under the single definition in the UK regime for 'safeguarding and administering' assets (Investments) belonging to other persons, which include the activity of arranging custody (unless the arrangement is with a qualifying custodian where an exclusion is available if certain conditions are met).[15]

34. As we have two separate Financial Services, some anomalies and ambiguities have arisen (which are addressed in Part D). However, such anomalies and ambiguities do not, themselves, present a case for not regulating the activity of Arranging Custody. Instead, risks (such as those noted in paragraph 35) associated with that activity alone can support (or not) retaining regulation.

35. The key risks that arise relating to arranging custody are not dissimilar to 'Arranging deals in Investments', in that, a firm may, for fees or commissions, arrange for customers to obtain custody services on inappropriate terms or circumstances. There is also a risk an arranger may, if holding Client Investments, misappropriate or co-mingle such assets with its own or those of other customers. Therefore, we propose to retain current regulation of 'Arranging Custody' as a Financial Service to address such risks (for example through the application of Client Asset controls in COB which apply to firms Arranging Custody – see draft COB Rule 6.11.1(c) in Appendix 3), rather than remove such activities from regulation.

36. We considered whether it is appropriate to combine the Financial Service of 'Arranging Custody' with that of 'Providing Custody' as under the UK regime. This would result in firms 'Arranging Custody', which are currently subject to prudential regulation as PIB Category 4 firms, becoming subject to a higher level of prudential regulation as firms 'Providing Custody', which are PIB Category 3C firms.

37. We do not propose to combine these two Financial Services because we do not think that the risks associated with a firm Arranging Custody are as significant as for a firm Providing Custody.[16]

Issues for consideration

Q1: Do you have any concerns relating to our proposals to continue to regulate 'Arranging deals in Investments' as a stand-alone discrete Financial Service? If so, what are they, and how should they be addressed?

Q2: Do you have any concerns relating to our proposal to retain regulation of 'Arranging Credit' as a Financial Service? If so, what are they, and how

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Importantly, under the UK definition, it is immaterial that the assets safeguarded or administered are transferred to a third party subject to a commitment given by that third party that the assets will be replaced by equivalent assets at a specified time or on demand by the Client.

[15] To benefit from the exclusion relating to third party qualifying custodians, the conditions that must be satisfied are that the custodian undertakes to the client obligations no less onerous than those of the firm undertaking to safeguard and administer investments for the client, and the qualifying custodian itself is either conducting the business of safeguarding and administering investments in the UK or doing so as an exempt person.

[16] For example, the systems and controls of a firm Providing Custody need to be designed to address operational and other risks which are associated with the direct or indirect holding of assets of clients for the purposes of providing safe custody, which is not the case with a firm Arranging Custody.

should they be addressed?

Q3: Do you have any concerns relating to our proposal to separate 'arranging credit' from the Financial Service of 'Arranging deals in Investments'? If so, what are they, and how should they be addressed?

Q4: Do you agree with our proposal to continue to regulate 'Arranging Custody' as a stand-alone Financial Service? If not, what are your reasons?

Q5: Do you have any other concerns relating to the regulation of arranging activities relating to Investments, credit and custody which need to be addressed? If so, what are they, and how should they be addressed?

(b) Should we continue to regulate 'Advising on credit' as a Financial Service?

38. Our regime relating to 'advising on credit' provides a significant layer of client protection. While the lender may undertake due diligence about the borrower's capacity to repay the debt, this is not a substitute for an adviser's assessment of the merits of a particular borrower obtaining credit, which would need an assessment of the circumstances, needs and objectives of the particular borrower.[17] Therefore, the activity of 'Advising on credit' warrants regulation as a Financial Service. However, to maintain consistency with the approach adopted relating to 'Arranging credit', this activity warrants having its own Financial Service, rather than being coupled with Advising on Investments.

39. We propose to create a composite Financial Service, called 'Arranging and Advising on Credit', covering both 'Arranging credit' and 'Advising on credit' to:

(a) provide regulation based on the relevant financial sector – i.e. credit, as opposed to investments; and

(b) not proliferate Financial Services unnecessarily.

(See draft GEN Rule 2.28.1 in Appendix 2).[18]

Issue for consideration

Q6: Do you have any concerns relating to our proposal to separate 'Advising on credit' from the Financial Service of 'Arranging deals in Investments'? If so, what are they, and how should they be addressed?

(c) How should the arranging and advising activities relating to Long-Term Insurance be regulated?

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[17] Advising on credit and investments, and similarly on insurance, involves substantially the same procedures as required for a 'suitability' assessment under COB Rule 3.4.2. This is because, to give advice on the merits of a Person entering into a transaction relating to obtaining credit, making an investment or buying insurance, a firm needs to undertake an assessment of the needs, objectives and circumstances of the potential borrower, investor or policyholder. Therefore, such advice would tantamount to a suitability recommendation.

[18] We have a precedent for doing so under 'Insurance Intermediation' which covers advising, acting as agent and arranging relating to insurance.

40. ‘Arranging’ and ‘advising’ activities relating to Long-Term Insurance (LTI) are currently treated as Investments and regulated under the Financial Services of ‘Arranging deals in Investments’ and ‘Advising on financial products’.[19]

41. Although LTIs are a sub-set of life-insurance,[20] advising and arranging activities relating to LTIs are regulated as Investments because such products are often investment-linked insurance products. Under other regimes we benchmarked, including under the EU regime, intermediation activities relating to investment-linked insurance products attract investment-related regulation.[21] Therefore, we do not propose to alter the current regulation of intermediation activities relating to LTI under ‘Arranging deals in Investments’ and ‘Advising on financial products’.

42. However, we have identified an issue relating to the regulation of LTIs, namely whether, and to what extent, the activity of ‘acting as agent’ relating to LTIs is regulated.

How should the activity of ‘acting as agent’ relating to LTIs be regulated?

43. Under the definition of Insurance Intermediation, which applies to all insurance other than LTI, all three activities of intermediation, i.e. ‘advising’, ‘arranging’ and ‘acting as agent’ are regulated activities.[22] Given that LTIs are a subset of contracts of insurance, these three activities, so far as they relate to LTI, need to be regulated.

44. However, under the current regime, while LTIs are covered under the definitions of ‘Arranging deals in Investments’ and ‘Advising on financial products’, the Financial Service of ‘Dealing in Investments as agent’ does not apply to ‘acting as agent’ in respect of an LTI. This raises an inference that ‘acting as agent’ relating to LTI may not be a regulated activity, which is not true.

45. Although not stated explicitly, the definition of Insurance Intermediation captures the activity of ‘acting as agent’ relating to LTI. This is because, while the Financial Services of ‘advising’ and ‘arranging’ are expressly excluded from the definition of Insurance Intermediation (see GEN Rules 2.19.6 and 2.19.7), the activity of ‘acting as agent’ relating to LTI is not expressly excluded. As a result, a firm which is acting as agent for another person to buy LTI will require a Licence as an Insurance Intermediary. If a firm is acting as an Insurance Agent of an insurer when selling LTI for that insurer, it could do so under an Insurance Management Licence or an Insurance Intermediation Licence.[23]

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19 See GEN Rules 2.9.1(4) and GEN Rule 2.11.1(3).

20 See the GLO definition of Long-Term Insurance (LTI). Under that definition, insurance contracts relating to certain classes of life insurance products defined in GEN Rule A4.1.2 where the payments are to be made upon the death of the insured, sickness of the insured or members of his family or the marriage or birth of a child of the insured are classified as LTI if such contracts are expressed to be in force for more than one year.

21 For example, under the EU regime, MiFID requirements apply to investment linked insurance products. Similarly, under the UK regime, investment-linked insurance products attract more stringent regulation as investments.

22 See GEN Rule 2.11.1.

23 A Person can act as agent of an insurer or policyholder. Under the changes to the insurance regime resulting from CP103, we introduced GLO Module definitions of the terms ‘Insurance Agent’ and ‘Insurance Broker’.

46. Although it seems somewhat anomalous, we considered it appropriate to continue the current position (as noted in paragraph 45) because 'Dealing in Investment as agent' does not provide an appropriate form or level of regulation for the activity of 'acting as agent' relating to the buying and selling of LTIs, because:

(a) LTIs are generally not frequently tradable instruments like other Investments (such as shares, bonds and units of Funds); and

(b) as a consequence of (a), acting as agent in respect of LTIs does not give rise to the same regulatory risks as 'Dealing in Investments as agent'.[24]

47. Therefore, we propose to retain the current position where a firm acting as agent for a buyer of LTI (i.e. an Insurance Broker) will generally need an Insurance Intermediation Licence, while a firm acting as agent of a seller of LTI (i.e. an Insurance Agent) will be able to do so under either an Insurance Intermediation or Insurance Management Licence.

48. There may be some confusion as to whether a firm acting as agent relating to LTI would need to be licensed at all. To remove such ambiguity, we propose to include Guidance to that effect under the definitions of Insurance Intermediation and Insurance Management (see draft Guidance item 4 under GEN Rule 2.19.1 in Appendix 2).

Issues for consideration

Q7: Do you have any concerns relating to our proposal to retain the current regulation for firms 'acting as agent' relating to LTI under Insurance Intermediation and Insurance Management? If so, what are they, and how should they be addressed?

Q8: Do you have any other concerns relating to regulation of LTI? If so, what are they, and how should they be addressed?

(e) Should any changes be made to the activities excluded from regulation as arranging and advising?

49. We considered a few changes to the current exclusions as discussed below, whilst retaining most of the other exclusions unchanged.

Exclusion for Representative Offices[25]

50. The current definition of 'Arranging credit or deals in Investments' expressly excludes[26] 'the arrangements of the kind described in Rule 2.26.1 (i.e. Rep Office activities) that constitute marketing'. However, GEN Rules 2.2.10 and 2.26.2 already enable Authorised Firms to conduct the kind of activities which fall within the definition of Operating a Representative Office. So we propose to remove the express exclusions

[24] This is reflected in the fact that 'Dealing in Investments as agent' attracts a higher prudential category (as a PIB Category 3A firm), compared to 'acting as agent' relating to other insurance, which attracts prudential regulation as a PIB Category 4 firm.

[25] See GEN Rule 2.9.1(3)(b).

[26] The definition of 'Insurance Intermediation' in GEN Rule 2.19.1(5) also contains such an exclusion.

in GEN Rules 2.9.1(3)(b) and 2.19.1(5) (see Appendix 2).

Exclusion for transactions to which the arranger is a party [27]

51. There is an exclusion (as under the UK regime) for arrangements with a view to transactions where the arranger is itself a party to such a transaction. The rationale for this exclusion is that 'arranging' activities generally facilitate other parties to transact, and a person cannot be both the 'dealer' (where it is a party to the transaction), and the 'arranger', where it is merely the party intervening to arrange a deal between a dealer and the customer.

52. We propose to retain this exclusion as it is a critical element of arranging, and distinguishes it from the conduct of the Financial Service which is arranged for. For example, a firm 'arranges' a transaction for a customer when it facilitates the customer to buy shares by placing an order with a broker. The broker, 'deals in securities as agent' by carrying out the purchase/transaction, to which it is a party. However, we propose to make a change to that exclusion to better clarify the intent of that exclusion (see draft GEN Rule 2.9.2 in Appendix 2).[28]

Exclusion for mere communication channel providers [29]

53. We propose to retain this exclusion and also include a similar exclusion for Arranging and Advising on Credit. Further, to provide greater clarity relating to the scope of this exclusion, we propose to add Guidance along the lines in the previous paragraph.

Issues for consideration

Q9: Do you agree with our proposal to retain most of the current exclusions, subject to a few refinements and clarifications as noted above? If not, what are your reasons?

Q10: Are there any other concerns relating to current exclusions which we have not identified? If so, what are they, and how should they be addressed?

Part D: Proposals to promote greater clarity relating to the regulation of arranging and advising activities

54. We have identified some confusion relating to:

(a) how different types of intermediation activities differ from each other (for example, the distinction between 'arranging' and 'acting as agent'); and

(b) how arranging differs from the substantive activities to which arranging relates.

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[27] See GEN Rule 2.9.2.

[28] GEN Rule 2.9.1(1) refers to arrangements with a view to another Person, whether as principal or agent, buying, selling … an Investment. The words 'with a view to' bring within the scope of arranging such arrangements which do not result in a transaction, provided the objective of the arrangement is to enable other people to transact.

[29] See GEN Rule 2.9.3.

The difference between 'acting as agent' and 'arranging'

55. 'Arranging' and 'acting as agent' have a significant overlap, because both activities relate to the activities of buying and selling of financial products/instruments, and the processes involved are similar.

56. However, the primary distinction between 'acting as agent' and 'arranging' is that a person acting as agent has the authority to bind its principal (i.e. to execute transactions or otherwise commit its client/principal to a transaction), whereas a person 'arranging' for another person to buy or sell Investments or insurance is a third party facilitator of a transaction or potential transaction, with no authority to bind any one of the parties to the transaction, or commit them to the transaction.

57. We propose to include Guidance to clarify this distinction, so far as it relates to Arranging deals in Investments, Insurance Intermediation and Insurance Management (see the proposed Guidance under draft GEN Rule 2.9.1 in Appendix 2).

The difference between 'Arranging Custody' and 'Providing Custody'

58. 'Providing Custody'[30] involves the activities of 'safeguarding and administering' Investments belonging to another person, whereas 'Arranging Custody'[31] involves arranging one or more persons to carry on the activities defined as 'Providing Custody'.

59. Arranging Custody is an activity of an intermediary. Therefore, an arranger has no direct responsibility to clients for safeguarding and administering their assets (money or Investments) where it arranges for (i.e. facilitates) such clients to obtain custody services from an appropriately licensed or regulated custodian.

60. In contrast, a person Providing Custody is legally accountable to clients for safeguarding and administering their assets. This does not mean that the person Providing Custody necessarily has to hold client assets in its name or itself. It may appoint a third party provider as its agent to hold the assets. But nevertheless it remains accountable to the clients for safeguarding the assets entrusted to it.[32]

61. As the firm Providing Custody remains accountable to clients for safeguarding or administering their assets, we require such firms, when outsourcing or delegating custody to third party service providers, to undertake due diligence. They are also subject to Client Asset provisions in COB.[33] This accountability to clients of a person Providing Custody distinguishes that Financial Service from 'Arranging Custody', where the firm undertaking the latter is not accountable to the client for the safeguarding or administering of client assets.

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30 See GEN Rule 2.13.1.

31 See GEN Rule 2.14.1.

32 This means a firm Providing Custody remains liable to its Clients where a Third Party Custodian it has appointed fails to perform its duties properly. In such a case, Clients of the firm have a direct right of action (recourse) against the firm which undertook to Provide Custody. The firm itself may pursue a right of action against the Third Party Custodian under its contract with that custodian.

33 See COB section 6.11.

62. Factors that indicate whether a firm is 'Arranging Custody' for a client or 'Providing Custody' to a client, especially where there is a third party service provider involved, are:

(a) in whose name the Client Asset Accounts are opened; and

(b) who has the authority to control and operate such accounts.

63. If the firm opens Client Accounts with a bank in its own name, and has the power to operate/control such accounts, this is generally an indicator that the firm is Providing Custody. A firm Arranging Custody will not be a party to an agreement with a custodian and the client obtaining custody, and will not control or operate any accounts in which client monies or Investments are held by the custodian.

64. To promote certainty and clarity, we propose to include Guidance to the above effect in our Rules (see the proposed Guidance under GEN Rules 2.13.1 and 2.14.1 in Appendix 2).

Do firms Arranging Custody and Providing Custody 'hold or control' Client Assets?

65. This issue arises because the Client Asset provisions in COB (in section 6.11) apply both to firms Providing Custody or Arranging Custody and to firms which 'hold or control' Client Assets. This has given rise to an ambiguity as to whether firms Providing Custody or Arranging Custody are also 'holding or controlling' Client Assets (as an integral part of their activities relating to Providing or Arranging Custody). If they do, a separate reference to 'holding or controlling' Client Assets would seemingly not be necessary.

66. A person Providing Custody would generally need to 'hold' and/or 'control' Client Assets to be able to Provide Custody, which involves 'safeguarding and administering' Client Assets. However, as there are firms other than those which Provide Custody which may 'hold or control' Client Assets (for example, firms dealing as agent and firms Managing Assets[34] on a discretionary basis or acting as trustee of a Fund), the Client Asset provisions in COB need to differentiate between Providing Custody and 'holding' or 'controlling' Client Assets. Therefore, the distinct reference to 'holding or controlling' Client Assets in COB Rule 6.11.1 does not give rise to an inference that firms Providing Custody do not hold or control Client Assets.[35]

67. Although firms Providing Custody hold or control Client Assets, firms Arranging Custody do not necessarily do so (except where they also conduct other Financial Services such as 'dealing as agent'), as they are not a party to a contract to Provide Custody. The inclusion of Arranging Custody as a Financial Service attracting Client Asset provisions seems to be a legacy issue. Under the UK regime, arranging custody is included as part of the regulated activity of 'safeguarding and administering' Investments.

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[34] See GEN Rule 2.10.1.

[35] Firms 'Dealing in Investments as Agent' also safeguard and administer Client Assets, as do those firms 'Providing Trust Services'. These firms do not need a Providing Custody Licence to carry out their Financial Services as dealers or trustees.

68. As Arranging Custody in itself does not require the arranger to either hold or control Client Assets under our regime, we propose to remove Arranging Custody from the Client Asset provisions in COB section 6.11, with the exception of:

(a) the obligation to undertake due diligence relating to non-DIFC custodians, with whom the firm arranges for its customers to obtain custody services – to ensure that firms providing custody pursuant to such arrangements are regulated at a comparable level as under the DFSA regime; and

(b) the obligation to make disclosure under COB App 6.7.1(1) if the custodian is located outside the DIFC.

(See draft COB Rules 6.11.1(c), 6.11.2(3) and COB App 6.5.1A in Appendix 3)

Other areas of ambiguity

69. In addition to the ambiguities noted above, we have identified other areas relating to the Financial Services dealing with arranging and advising activities, which warrant further Guidance (see the proposed Guidance under draft GEN Rules 2.9.1, 2.13.1, 2.14.1 and 2.28.1 in Appendix 2).

Issues for consideration

Q11: Do you have any concerns relating to the proposals to provide greater clarity between 'arranging' and 'acting as agent' and also, between 'Arranging Custody' and 'Providing Custody'? If so, what are those concerns and how should they be addressed?

Q12: Do you agree with our proposals to remove the application of the Client Assets provisions in COB to firms Arranging Custody? If not, what are your reasons?

Q13: Do you have any concerns relating to the proposed Guidance relating to arranging and advising activities referred to above? If so, what are they, and how should they be included?

Q14: Are there other areas that warrant clarification? If so, what are they, and how should they be clarified?

Part E: Proposals relating to Representative Offices

70. We have identified through our supervisory work that some Representative Offices (Rep Offices) could be overstepping the boundaries of their authorisation. This is more likely to be the case due to a perceived lack of clarity between the activities of Rep Offices and firms arranging and advising, rather than a deliberate attempt at regulatory arbitrage.

71. A Rep Office's remit is to 'market one or more financial services or financial products which are offered in a jurisdiction outside the DIFC'. Under the REP module, a Rep Office can only market financial services and financial products offered by its own head office, and those of its Group members, outside the DIFC.

72. A financial product is defined as 'an Investment, a Credit Facility, a Deposit, a Profit Sharing Investment Account and Contracts of Insurance' (both LTI and other

insurance).

73. The term 'marketing' is defined as 'providing information' (to potential customers) about financial products or financial services offered by its head office or by a Group member outside the DIFC, engaging in promotions (such as holding events and seminars relating to those financial products and services) and making introductions, i.e. referrals, of (prospective customers) to its head office or a Group member, as is relevant.

74. A Rep Office is expressly prohibited from advising on financial products and financial services, as well as receiving and transmitting orders in relation to them (which are activities of arranging firms).

Is there an overlap between 'advising' and 'arranging' activities on the one hand and Rep Office activities on the other?

75. A Rep Office is prohibited from advising. Only firms with an authorisation as an adviser can give advice.

76. A Rep Office can only 'market' financial products or financial services of its related parties by giving information relating to the relevant financial product or financial service (as opposed to the merits of a particular investor entering into a transaction in relation to a financial product or insurance – which amounts to advising).

77. Information which a Rep Office can give needs to be general information about a financial service or financial product/insurance. Such information can include:

(a) who the provider of the relevant financial product or financial service is, and where that provider can be contacted;

(b) in the case of credit, information about the terms of credit, including any information relating to collateral required;

(c) in the case of insurance, what type of risks are covered or excluded under it;

(d) if LTI or other Investments, what types of benefits are available, and also any risks associated with the relevant Investment; and

(e) how charges or premiums are calculated.

78. Information ceases to be 'general information' if there are any suggestions about the merits of the relevant financial product or financial service to a particular person, in light of that person's circumstances, needs or objectives. If this happens, then it becomes advice, as it contains views on the merits of a particular investor or policyholder entering into a transaction (such as to buy or sell the relevant product).

79. A Rep Office is prohibited from receiving and transmitting orders in relation to a financial product. Generally, receiving and transmitting orders are activities which a firm can undertake as part of 'Arranging credit or deals in Investments' or 'Insurance Intermediation', for which they need to be authorised.

80. A Rep Office is permitted, as part of its marketing activities relating to financial

products or financial services, to make introductions or referrals of potential clients to its head office or a Group member (outside the DIFC). Similarly, all Authorised Firms can make referrals, giving rise to an overlap between the activities of Rep Offices and other firms.[36]

81. We have found, through our supervisory experience, that some Rep Offices engage in activities which are likely to exceed the narrow remit within which they are permitted to operate. Examples of such activities include:

    (a) opening and closing bank accounts and processing withdrawals for customers; and

    (b) handling client complaints and on-going inquiries relating to the financial products and financial services offered by the head office or Group member.

82. To address concerns relating to Rep Offices exceeding their boundaries, we have considered a number of options:

    (a) Option 1 – removing Rep Office Licences;

    (b) Option 2 – creating a new bespoke Licence for Rep Offices;

    (c) Option 3 – making a more drastic reduction in the scope of a Rep Office Licence;

    (d) Option 4 – restricting the life of a Rep Office Licence to some specified period; or

    (e) Option 5 – retaining the Rep Office Licence and enhancing clarity about its scope.

Option 1 – Remove Rep Office Licences

83. There are two ways in which Rep Office Licences can be removed:

    (a) by not regulating the activities conducted by a Rep Office as a Financial Service; or

    (b) by including Rep Office activities as part of the Financial Services of arranging or advising, as appropriate.

84. We do not think removing regulation of the activities of a Rep Office as a Financial Service altogether is warranted, given the reputational risks arising if marketing activities are conducted in the Centre in an unregulated environment. Further, monitoring whether persons conducting such activities are breaching the Financial Promotions prohibition, or encroaching into the areas of arranging and advising activities, would become harder to supervise than now.

[36] Authorised Firms, when making introductions or referrals, cannot hold out that they are themselves providing the relevant financial product or financial service. If they do, they could run the risk of contravening the scope of their Licence if the activities of the firms to which the referrals are made are wider than the scope of the referring firm's Licence.

85. If we were to adopt the alternative approach of including Rep Office activities within existing regulation for arrangers and advisers, it could result in:

(a) including, under the Financial Service of advising on financial products, the activity of providing information on financial products. This would result in having two types of advice; advice about the merits of a particular person, in his personal capacity, entering into a transaction and general advice about financial products, which contains information about financial products;

(b) including under the Financial Services of arranging, the activity of making introductions or referrals, on the basis that these activities facilitate potential customers to transact with product providers; and

(c) leaving promotional activities to be regulated under the Financial Promotions regime, where Authorised Firms are permitted to undertake such activities.[37]

86. We do not propose this option, at least now, given that the risk of Rep Offices exceeding the scope of their Licence can be addressed through measures which we have identified below.

Option 2 – Create a new bespoke Licence for Rep Offices

87. Option 2 requires increasing the current level of regulation of Rep Offices without raising it to the same level of regulation as applicable to firms arranging and advising. The current regulation of Rep Offices, which does not attract prudential regulation, reflects the absence of prudential risks arising from the activities of Rep Offices.

88. For similar reasons, a Rep Office is required to comply with only a very limited number of requirements in the other parts of the DFSA Rulebook, when compared to an arranging/advising firm.[38] The REP module itself, which contains bespoke Rules, is also very narrow, confined to:

(a) four Principles for the firms (relating to integrity, due care and diligence, resources and relations with the regulator);

(b) requirements for fitness and propriety of the firm and its Principal Representative;

(c) disclosure of regulatory status as a Rep Office;

(d) clear, fair and not misleading requirement for its marketing material;

(e) a prohibition against holding or controlling others Persons' funds (except to the extent necessary to deal with its ordinary business operating expenses); and

(f) limitations on the type of Foreign Funds it can market (mirroring CIF provisions).

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[37] See GEN Rule 3.4.1(1).

[38] Such as the definitional provisions, provisions relating to Financial Promotions and supervision provisions in chapters 2, 3 and 11, and AML provisions with regard to the reporting of any suspicions of ML and TF activities.

89. The current level of regulation appears to be proportionate and commensurate with the limited Rep Office activities, provided they do not exceed the scope of their Licence. If we were to increase the scope of activities of a Rep Office to justify an increase in regulation (to create a new prudential 'Category 4 type' Licence for Rep Offices), it becomes hard to maintain a distinction between a Rep Office's activities and those of an arranger or adviser. Therefore, logically and practically, there is little regulatory space to create a new type of Rep Office Licence with expanded scope, whilst also retaining the existing Licences for arrangers and advisers.

Option 3 – make a more drastic reduction in the permitted activities of a Rep Office

90. This option reflects practices adopted in other jurisdictions benchmarked. For example, under the UK regime, a Rep Office does not conduct regulated activities which require a financial services licence. Instead, a Rep Office can only carry on limited activities in the UK without contravening the financial services and the financial promotions prohibitions. The activities Rep Offices are permitted to conduct are limited to:

(a) developing and maintaining relationships with correspondent banks to support the head office activities;

(b) increasing the institution's profile within the market;

(c) acting as a point of contact for, and a source of information on, the institution;

(d) reporting to the head office on business trends and opportunities in the UK; and

(e) providing information to the head office about developments in financial markets, tax matters, and changes in the UK's supervisory regime.

91. If we were to follow this option, a Rep Office would not be considered as carrying on any of the current Financial Services. Therefore, it would not be able to undertake any marketing or referral activities. This option would also remove the concerns raised by advising/arranging firms that Rep Offices are exceeding the boundaries of their Licences, and thereby gaining an unfair advantage (i.e., Rep Offices conducting similar activities at a much lower cost).

92. However, such a restriction has a significant disadvantage. The DFSA will no longer have a regulator-licensee relationship[39] with a Rep Office and, as such, monitoring their activities to ensure they do not contravene either or both the Financial Services and Financial Promotions prohibitions would become harder.

Option 4 – restrict the life of a Rep Office Licence

93. Option 4 entails restricting the life of a Rep Office Licence to three years, or some other specific period. This is based on considerations that Rep Offices are generally established to enable overseas financial institutions to test the water in the relevant jurisdiction in terms of their business potential, and to monitor local markets. Therefore, at the end of a specified period, they should be able to determine whether

[39] Except, perhaps, as a DNFBP, for the purposes of AML.

to upgrade their Licence, as appropriate, or cease to have a presence in the DIFC.

94. There are some jurisdictions which do this. For example, both Singapore and the UAE grant Rep Office Licences for two years, but give the holders the option to renew. We do not consider imposing such a restriction on the life of a Rep Office is warranted, as we have only relatively recently established this regime, and the concerns so far identified seem capable of being addressed as discussed below.

Option 5 – retaining Rep Office Licence and enhancing clarity of its scope

95. This option entails retaining the Rep Office Licence in its current form, with measures to ensure that the scope of it is clear and easy to monitor and supervise. For this purpose, we propose a number of measures:

(a) issue more detailed Guidance relating to the permitted activities of a Rep Office (coupled with Guidance clarifying the scope of 'arranging', 'advising' and 'acting as agent' proposed earlier under paragraph 77);

(b) undertake outreach programmes for Rep Offices around the new Guidance; and

(c) remove any requirements in the current regime which are outdated or ambiguous and, so, open to abuse as noted below.

96. For example, REP Rule 4.3.1 prohibits a Rep Office from holding or controlling money or other property belonging to another Person 'except to the extent that this is necessary to deal with its ordinary business operating expenses'. We believe that a reference to monies or other property belonging to other Persons is too wide. This may be interpreted as permitting a Rep Office to hold money or assets which belong to clients of its head office. We propose to retain the current prohibition without the exception, and include Guidance that a Rep Office could maintain an operating account for business purposes provided it does not contain any monies other than proprietary funds/assets (see draft REP Rule 4.3.1 and Guidance in Appendix 4). We also propose to make certain refinements to REP Rule 4.6.5(2) to ensure that marketing material that can be distributed by a Rep Office remains general information (see draft REP Rule 4.6.5(2) in Appendix 4).

Comparative analysis of the options

97. None of the above options provide a perfect solution to the regulatory concerns about the potential for Rep Offices to exceed the scope of their Licences. Having allowed Rep Offices to be established in the DIFC, the removal of this category altogether, without pursuing other ways to mitigate the risk of possible contravention of the boundaries of such Licences, seems difficult to justify.

98. Before turning to the more drastic measures canvassed under other options, such as removing this category of Licence altogether, we propose to adopt Option 5 (see also the more detailed Guidance we propose to include in relation to Rep Offices under draft GEN Rule 2.26.1 in Appendix 2).

99. Further, to promote more effective compliance, we propose that the annual regulatory return of a Rep Office include a declaration by the Principal Representative that he has taken all reasonable steps to ensure that the Rep Office has not exceeded the

boundaries of its Licence and he is also not aware of conduct that would constitute exceeding the limits of its Licence by the Employees of the Rep Office, during the relevant year.[40]

Issues for consideration

Q15: Do you have any concerns relating to our proposal to adopt option 5 – which is to retain the Rep Office Licences? If so, what are those concerns and how should they be addressed?

Q16: Do you have any concerns relating to the Guidance we propose to provide clarity relating to the scope of a Rep Office Licence? If so, what are those concerns and how should they be addressed?

Q17: Are there other areas of Guidance needed? If so, what are they, and why should they be included?

Q18: Do you have any concerns about our proposals to impose an obligation on the Principal Representative to make an annual declaration of compliance? If so, what are those concerns, and how should they be addressed?

Q19: Are there other areas that warrant clarification? If so, what are they, and how should they be clarified?

Part F: Proposals relating to Financial Promotions

100. We have not undertaken a comprehensive review of the Financial Promotions regime. We are also not aware of any concerns to warrant such a review. However, given that Rep Offices are permitted to conduct promotions relating to financial products and financial services of related parties under their Licence, we have considered whether there are any concerns or issues arising in the context of the Financial Promotions regime.

Can a Rep Office conduct Financial Promotions to the same extent as another Authorised Firm?

101. All Authorised Firms are permitted under their Licence to make Financial Promotions.[41] Similarly, all Authorised Firms can approve communications of other financial service and financial product providers, so that such communications become 'exempt Financial Promotions' and allow the relevant financial service and product providers or their agents, although not regulated firms in the DIFC, to undertake Financial Promotions in or from the DIFC.

102. As a Rep Office is an Authorised Firm, it can *prima facie* undertake any Financial Promotions or approve communications of unregulated persons as 'exempt Financial Promotions'. However, a Rep Office's ability to do so conflicts with the narrow area of promotions permitted under the Rep Office's regime, which confines Rep Office promotional activities to financial services and financial products of its head office or a

[40] Under the current proposals relating to electronic forms, provision is already made for a similar declaration.
[41] See GEN Rule 3.4.1(1).

Group member.

103. The restrictions applicable to promotions which a Rep Office can conduct need to prevail over the wider ambit of Financial Promotions allowed for other Authorised Firms because:

(a) if the wider ambit were to prevail, the restrictions imposed on a Rep Office would become redundant; and

(b) there is little policy justification for allowing a Rep Office to undertake the full range of Financial Promotions, given that they are subject to less regulation than other Authorised Firms.

104. We propose to remove this anomaly so that the promotional activities of a Rep Office are confined to the permitted activities of a Rep Office under the current regime, i.e. promotional activities relating to the financial services and financial products of its head office or a member of its Group. This would also address concerns raised by some Authorised Firms that Rep Offices are currently permitted to undertake activities similar to theirs at a lower cost (see draft GEN Rule 3.4.1(1A) and the proposed Guidance item 14 under draft GEN section 2.26 in Appendix 2).

Are there any other changes needed?

105. We have stated in Guidance item 6 in GEN Rule 3.2.1 that, depending on the nature and scale of the activities, if a Person makes Financial Promotions on a regular basis or for a prolonged period while physically located in the DIFC, for example, by way of a booth, meetings or conferences, the DFSA may consider such activities as constituting the carrying on of a Financial Service, such as Operating a Rep Office. We have also stated that in the DFSA's opinion, 'a regular basis' means anything more than occasional and 'a prolonged period' usually means more than three consecutive days.

106. These restrictions are critical to:

(a) ensure persons who do not have a permanent place of business in the DIFC do not undertake, in or from the DIFC, Financial Promotions in a manner that contravenes the Financial Promotions or Financial Services prohibitions. If they conduct Financial Promotions in or from the DIFC with system, regularity and continuity (the common law test), they are doing so by way of business, and would need to be appropriately licensed; and

(b) maintain a clear distinction between the permitted activities of Authorised Firms and Rep Offices as persons subject to DFSA regulation, and others who are not subject to DFSA regulation, but are permitted to conduct sporadic financial promotions within the narrow remit permitted under the Financial Promotions regime.

107. Although critically important, as they are currently Guidance, these limits do not have the same binding force as Rules. Therefore, we propose to further refine these limits and turn them into a Rule (see draft GEN Rule 3.4.1(2) and (4) in Appendix 2).

Issues for consideration

Q20: Do you have any concerns relating to our proposal to restrict Rep

Offices ability to approve 'exempt Financial Promotions' so far as they relate to the financial products and financial services offered by its head office/Group member outside the DIFC? If so, what are those concerns and how should they be addressed?

Q21: Do you have any concerns relating to our proposals to elevate to Rule level current Guidance relating to the parameters of 'exempt Financial Promotion'? If so, what are those concerns and how should they be addressed?

Q22: Are there other issues or areas that warrant clarification? If so, what are they, and how should they be clarified?

Part G: Transition

108. There are a number of ways in which the above proposals, if implemented (following public consultation), could affect the current activities of firms conducting arranging and advising activities, Rep Offices and also those conducting Financial Promotions without having a permanent place of business in the DIFC.

109. For example:

(a) an Authorised Firm conducting 'Arranging and Advising on Credit' (the proposed new Financial Service), would need a new type of a Financial Service Licence. If a firm is already licensed to carry on arranging and advising on credit, we propose to amend its existing Licence to an 'Arranging and Advising on Credit' Licence upon the implementation of the new regime without the need to go through any fresh approval process. We also propose, to the extent current documentation (such as letterheads and other material) does not contain a reference to 'Arranging and Advising on Credit', to allow firms a period of six months from the implementation before they must use new communication material.

(b) Some Authorised Firms may need Licences for a different type of activity than they currently hold. We would generally allow a period of six months for the firms to complete the necessary formalities to obtain the right type of Licence, which would need the usual assessment relevant to the type of Financial Service involved.

(c) Rep Offices which act beyond the scope of their Licences, as would be clarified under these proposals, would need to cease such activities immediately. No transitional relief is proposed.

(d) Entities which conduct Financial Promotions without a permanent place of business in the DIFC may also need to consider whether they could continue such activities. If they want to conduct such activities with system, regularity and continuity, they may need to apply for at least a Rep Office Licence (provided they are undertaking Financial Promotions relating to their own or Group financial services or financial products). We will not consider any transitional relief to allow continuation of Financial Promotions in breach of the regime.

110. We are seeking comments on whether there are any other circumstances in which

transitional relief is needed, so that we can consider what additional transitional arrangements are appropriate. We have not included in the draft Rules accompanying the CP any transitional provisions.

Issues for consideration

Q23: Do you have any concerns regarding our proposals relating to transitional arrangements? If so, what are they and how should they be addressed?

Q24: Are there any other areas which need transitional arrangements which are not covered under paragraph 109? If so, what are they and why should they be addressed?

Part H: Other aspects

111. As we are considering a wide spectrum of regulated activities covering a range of Financial Services, we would like you to consider whether there are any issues of a significant nature which warrant being addressed, that are not dealt with in this paper.

Issue for consideration

Q25: Are there any other aspects relating to arranging and advising, Rep Office activities or Financial Promotions, which are not addressed in this paper? If so, what are they, and how should they be addressed?

Appendix 1 – Benchmarking

112. The activity of arranging deals in investments is a regulated activity in the jurisdictions we generally benchmark against, i.e. the UK as a proxy for the EU regime,[42] Australia, Hong Kong and Singapore, although the manner in which each jurisdiction regulates this activity is found to be somewhat different. For example, under the UK regime, which we have substantially followed, arranging deals in investments is a discrete regulated activity.[43]

113. In Australia, arranging is regulated as part of the financial service of 'dealing as agent', with bespoke regulation of arranging activities of insurance brokers.[44] Under the Singapore and Hong Kong regimes, the activity of 'arranging' is implicitly a part of 'dealing' as (agent) relating to securities and futures. With regard to insurance, arranging is expressly included as part of the activities of an 'insurance agent' or of 'an insurance broker'.

114. Under the UK regime, arranging credit is not included in the definition of the regulated activity of 'Arranging deals in investments'. However, there are distinctly separate 'arranging' activities relating to home finance related lending which are regulated as 'regulated activities' under the UK regime.[45]

115. There is also a specific category of lending that is regulated under the UK regime, called 'credit broking'.[46] Credit broking involves consumer credit (i.e. credit provided to individuals to purchase goods or services), and covers activities such as assisting borrowers to obtain credit and introducing prospective borrowers to credit providers.

116. Under the Australian regime, providing credit is regulated by APRA and arranging credit is not a discrete regulated activity. However, ASIC has responsibility for consumer credit related activities, and there are conduct standards applicable to providers of such consumer credit and those who act as intermediaries (e.g. credit representatives and credit brokers).[47]

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[42] Under the Insurance Distribution Directive (IDD), arranging activities fall under 'distribution', defined to include 'proposing or carrying out other work preparatory to the conclusion of contracts of insurance and assisting in the concluding and administration of such contracts.'

[43] Under the UK regime, there is a single definition of 'Arranging deals in investments'. 'Investments' are defined to include both 'securities' and 'relevant investments'. Relevant investments are then defined to include most types of insurance contracts. See Article 25 of the Regulated Activities Order ("RAO"). Although there is a common definition for 'arranging' for both securities and insurance, some of the conduct rules applicable to securities and insurance intermediaries under the UK regime are separately set out, particularly to address industry specific requirements (see ICOB for insurance conduct requirements).

[44] Under the Australian regime, 'Arranging a person to deal', – i.e. apply for, acquire, issue, underwrite (if a security or managed investment), vary or dispose of a financial product, is an activity that is regulated as the Financial Service of 'Dealing in a Financial Product'. Financial Products are defined to include securities, futures and insurance. Conduct rules are mostly common, with some variations to address industry specific requirements.

[45] See Articles 25A, 25B, 25C and 25E of the RAO. These are relatively recent additions to the UK regime.

[46] See Chapter 6A of the RAO.

[47] Under the Australian regime, margin lending is defined as a financial product, and dealing in (which includes arranging), and advising on, margin lending activities are regulated as a financial service.