

A stylized world map in shades of orange and yellow, overlaid on a grid of latitude and longitude lines. The map is centered on the Atlantic Ocean, showing the Americas on the left and Europe and Africa on the right.

# Credible Deterrence In The Enforcement Of Securities Regulation

**INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS**

**June 2015**

**Revised in October 2023**





This paper reflects the collective experience and expertise of the member jurisdictions of IOSCO's Committee 4 on Enforcement and the Exchange of Information.

The factors referred to in this paper highlight useful enforcement practices and powers adopted by various regulatory authorities around the world to promote and encourage credible deterrence of misconduct.

A reference, in this paper, to a specific regulator does not mean other regulators have not adopted similar powers or practices.

This paper has not been prepared, nor is it intended for use as either an assessment or benchmarking reference for securities regulators.

Certain authorities may consider rule proposals or standards that relate to the substance of this report. These authorities provided information to IOSCO or otherwise participated in the preparation of this report, but their participation should not be viewed as an expression of a judgment by these authorities regarding their current or future regulatory proposals or of their rulemaking or standards implementation work. This report thus does not reflect a judgment by, or limit the choices of, these authorities with regard to their proposed or final versions of their rules or standards.

# TABLE OF CONTENTS

<b>CREDIBLE DETERRENCE IN THE ENFORCEMENT OF SECURITIES REGULATION .....</b>	<b>6</b>
INTRODUCTION .....	6
THE CONCEPT OF DETERRENCE .....	7
FACTORS UNDERPINNING CREDIBLE DETERRENCE.....	8
<b>CREDIBLE DETERRENCE FACTORS .....</b>	<b>10</b>
<b>Factor 1: Legal certainty: Certain and predictable consequences for misconduct .....</b>	<b>10</b>
Legal and regulatory requirements .....	10
Explicit and effective laws .....	11
Transparency laws and procedures.....	11
Transparency of proceedings .....	13
Judicial and administrative competence .....	13
Avoiding regulatory arbitrage .....	14
<b>Factor 2: Detecting misconduct: By having access to good information .....</b>	<b>16</b>
Market Surveillance .....	16
Cross border surveillance .....	18
Reporting mechanisms for the public.....	19
Gatekeepers .....	21
Whistleblowers.....	22
Targeted programmes .....	24
Self-regulatory and industry supervisory groups.....	24
<b>Factor 3: Co-operation and collaboration to eliminate wrongdoer safe havens .....</b>	<b>27</b>
International .....	28
Domestic.....	30
Regulatory affiliations.....	33
<b>Factor 4: Investigation and prosecution of misconduct: Bold and Resolute enforcement.....</b>	<b>35</b>
Regulatory resolve .....	35
Comprehensive powers .....	37
Avenues for enforcement.....	42
Incentives, co-operation, and settlement .....	43
<b>Factor 5: Sanctions: Strong punishments - no profit from misconduct .....</b>	<b>46</b>
Setting of sanctions.....	47
Restorative measures .....	48
Individual accountability.....	50
Cost recovery.....	52
<b>Factor 6: Public messaging: Promoting public understanding and transparency .....</b>	<b>53</b>
Alerting investors .....	53
Transparent enforcement and accountability.....	54
Timely publication .....	56
<b>Factor 7: Regulatory governance: Good governance delivering better enforcement .....</b>	<b>58</b>
Governance .....	58
Prioritisation .....	60
Capacity.....	61
Strategy.....	61
Innovation .....	62
Specialised enforcement tools.....	62
Measuring effectiveness .....	64
Understanding behaviour.....	66
BIBLIOGRAPHY.....	67
COMMITTEE 4 MEMBERS .....	68

# Credible Deterrence in the Enforcement of Securities Regulation

## Introduction

1. The purpose of this paper is to identify and promote awareness of those factors that may credibly deter misconduct in securities and investment markets.
2. Misconduct in securities and investment markets has profound and far-reaching consequences for all levels of society. Consumers, investors, capital markets, institutions, national economies, and global financial systems are all impacted when the integrity of securities and investment markets are undermined by misconduct.
3. Deterrence is credible when rational persons who are contemplating engaging in misconduct decide not to do so because they assess that the prospects of being detected, investigated, and punished outweigh the benefits.
4. Strong regulation that holds individuals and entities accountable and deters misconduct promotes public confidence in financial services and is a key factor in the development of efficient markets, financial services, and economies.
5. Enforcement plays an important role in deterring misconduct and thereby promotes public confidence, consumer protection and market integrity. While other regulatory activities, such as authorisation and supervision, also have a strategic function in deterring misconduct, this paper focuses primarily on those factors that are within the remit of enforcement programmes.
6. Timely enforcement intervention and holding both individuals and entities accountable promote credible deterrence. By using new technologies and techniques bold regulators can enhance the effectiveness of detection and the efficiency of investigations.
7. Jurisdictions and regulators seeking to maximise deterrence within their regulatory frameworks may find some of the factors worthy of further consideration. The factors referred to in this paper are not weighted or ordered in any priority as each can contribute to deterrence in different ways. Further, the effectiveness of the factors may be influenced by the unique legal and regulatory characteristics of each jurisdiction, the political and economic framework, the specific facts, circumstances and nature of the conduct to be deterred and the social, cultural, and economic environment.
8. A successful credible deterrence strategy can modify behaviour and reduce securities law contraventions, which in turn increases investor protection and confidence thereby creating an environment in which fair and efficient markets can thrive.

## The concept of deterrence

9. Deterrence in securities regulation requires laws with well-defined and sufficiently serious penalties. The seriousness of the sanction should reflect factors such as recidivism, dishonesty, deliberateness, extensiveness, the amount of profit gained, or loss avoided and the quantum of investor harm.
10. In an ideal world all those who engage in misconduct would be detected, prosecuted and sanctioned appropriately and in a timely fashion. However, this is unachievable, so regulators need to adopt strategies that maximise the prospects of delivering credible deterrence in a risk-based environment. The greater the success of a regulator in achieving this, the greater the attractiveness to investors of the financial markets and financial services it regulates.
11. Deterrence is at the heart of the strategies of securities regulators whose objectives are to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation. There is no one-size-fits-all approach but whatever the regulatory model (twin peaks, integrated, industry-based or functional) and approach (risk, principles or rule-based) a common implied or explicit objective of enforcement programmes is credible deterrence.
12. In 1998, IOSCO issued its Objectives and Principles of Securities Regulation (IOSCO Principles), which set out a framework to achieve the objectives of regulation. The framework is comprised of principles to which regulators should aspire, including principles relating to enforcement and cooperation<sup>1</sup>. This paper complements the relevant IOSCO Principles by encouraging wider strategic thinking about how to achieve and maintain credible deterrence. It does not alter the IOSCO Principles or the Methodology which support the assessment of compliance with these IOSCO Principles.
13. Although this paper promotes deterrence in the context of enforcement, other regulatory activities such as authorisation, supervision, surveillance and compliance are important to deterrence strategies. They can be cost-effective regulatory tools because they may be less resource and time intensive than enforcement action. Moreover, they can prevent misconduct occurring before investors or the markets are harmed.
14. Authorisation is the gate keeper to the financial services industry and should prevent bad players from entering the industry. Supervision and surveillance monitor the conduct of those who participate in the industry. Supervisory and surveillance activities are useful sources of information. Together with compliance they can be effective mechanisms for preventing misconduct and detecting, mitigating and containing the effects of misconduct after it has occurred.
15. All regulatory functions, including authorisation, supervision, and enforcement, should work together to achieve deterrence in securities regulation. Proactive programmes, such as financial literacy programmes that enhance investor awareness, may be a part of a broader investor protection strategy but are not strictly part of the enforcement toolkit and are therefore not considered in detail in this paper.

---

<sup>1</sup> Objectives and Principles of Securities Regulation, June 2010, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf> and Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD359.pdf>

## Factors underpinning credible deterrence

### 16. Regulators can deter misconduct when they:

- a.) **enhance the quality of legal and regulatory frameworks to provide legal certainty.** The quality of legal and regulatory frameworks and the laws that underpin them play a prominent role in shaping behaviour by creating and enforcing a system of incentives and disincentives. Legal and regulatory frameworks that provide legal certainty promote the administration of justice and regulation and establish a platform upon which individuals and entities can organise their affairs in a manner that complies with the law and understand that if they act in a manner that is outside the law, they will be held accountable.
- b.) **detect misconduct by having timely access to good information.** Regulators who use mechanisms to detect misconduct in a timely way will create an environment in which those contemplating or involved in misconduct have an expectation that they will be caught. Regulators who have access to sources of intelligence providing real time information will be more likely to detect misconduct before it causes harm to investors or markets.
- c.) **co-operate and collaborate to eliminate safe havens and work together.** Potential wrongdoers may be deterred from engaging in misconduct when they know that securities regulators are working with criminal authorities and other domestic, national, and international agencies to strengthen their detection, investigation, prosecution and sanctioning capabilities. This sends the message that they cannot evade justice by operating cross-border because cross border regulatory counterparts are working together to ensure wrongdoers have no safe haven.
- d.) **rigorously and swiftly investigate and prosecute<sup>2</sup> misconduct.** Potential wrongdoers may be deterred from engaging in misconduct when they realise that regulators will hold them to account for their actions. Timely enforcement interventions can prevent investor detriment and harm to market integrity.
- e.) **impose sanctions that are effective, proportionate, and dissuasive.** Sanctions can be a deterrent to wrongdoing and recidivism when they are consistently and reliably applied and have a meaningful correlation to the gravity of the misconduct, the economic and social impact of the misconduct, the unjust enrichment of the wrongdoer and the cost to investors. When potential wrongdoers believe the cost of engaging in misconduct is greater than the reward, they may be dissuaded from engaging in it. Regulators who have and use an array of regulatory responses and sanctions are more likely to deter potential wrongdoers' involvement in misconduct.
- f.) **send strong public messages and promote public understanding and transparency.** Public messaging and understanding of regulatory mandates strengthen deterrence by informing would-be wrongdoers that misconduct will be detected, investigated, and sanctioned and that regulators are working together to enforce the law and hold individuals and entities accountable. Regulators who communicate their objectives, mandates and outcomes enhance the deterrent impact of enforcement activities. Public messages send a clear signal about the type of behaviour that is unacceptable and thereby help to set industry standards.
- g.) **evaluate and revise enforcement governance, strategy, priorities, and tools.** Regulators who continually evolve their enforcement strategies, by regularly reviewing their governance arrangements, prioritising and allocating resources and ensuring that enforcement tools are fit for purpose will be organisationally agile and more responsive to

---

<sup>2</sup> This paper uses the word prosecute to mean taking legal action against accused persons by securities regulators or other sanctioning authorities.

emerging risks. When regulation is well designed and regulators have well developed enforcement strategies, target and prioritise misconduct and have the tools to detect, rigorously investigate, prosecute and sanction wrongdoing, then potential wrongdoers are likely to consider that the detrimental consequences of engaging in misconduct will outweigh the benefit.

17. A further description of each of the seven factors, together with examples of useful powers and good enforcement practices adopted by securities regulators to deter misconduct is provided in this paper under ***Credible Deterrence Factors***.

## Credible Deterrence Factors

### Factor 1: Legal certainty: Certain and predictable consequences for misconduct

#### In brief

18. Laws that are certain and predictable, and allow individuals and entities to foresee, and be held accountable for the consequences of their actions, play a key role in deterring misconduct. Laws should be written, interpreted, and applied in a way that fosters legal certainty, so that individuals and entities can understand the laws and rules that apply to them, foresee the possible consequences of their actions and organise their affairs in a way that complies with obligations. It should be noted that enacting suitable laws will not be sufficient to deter misconduct if those laws are not enforced.
19. Deterrence of misconduct will be assisted by laws and regulations that:
  - a.) are clear, unambiguous, and foster legal certainty;
  - b.) are tailored to the jurisdiction;
  - c.) are transparent and help people to know and understand the obligations that apply to them;
  - d.) create appropriate avenues for the prosecution and remediation of misconduct; and
  - e.) provide for administrative and judicial decision makers who are informed, impartial, independent, and competent.

#### In detail

##### Legal and regulatory requirements

20. Unambiguous legal and regulatory requirements provide clarity about behaviour that is unacceptable. The content of legal and regulatory requirements should be tailored to the needs and characteristics of each jurisdiction, including the nature, size and complexity of its markets, the financial products and services offered in the market, and the legal, economic, cultural, political and social environments.
21. A tailored set of laws and regulations should provide regulators and administrative and judicial decision makers with a varied and robust range of powers and remediation tools to detect, investigate, remediate and sanction misconduct effectively.
22. To that end, laws and regulations should enable regulators to use administrative, civil (including civil penalty), or criminal (including quasi-criminal) powers for the remediation of misconduct and the imposition of sanctions.

#### EXAMPLES

Many jurisdictions have a range of avenues, including administrative, civil and criminal to prosecute and sanction misconduct. For example, the Securities and Exchanges Board of India (SEBI), the Securities and Futures Commission of Hong Kong (HK SFC) and the Australian Securities and Investments Commission (ASIC) have the power and flexibility to pursue both deterrent and remedial actions against market misconduct through a variety of routes including criminal prosecutions and administrative, disciplinary and civil penalty proceedings

## Explicit and effective laws

23. Unambiguous laws and regulations foster legal certainty and assist in deterring misconduct.
24. Whatever the regulatory design, (i.e., twin peaks, integrated, industry based or functional), the quality and effectiveness of legal and regulatory requirements are critical to strengthening regulation. Some regimes adopt a *principles* or *outcomes* based approach to regulation that relies on broad but well-defined principles of acceptable behaviour, e.g., the obligation to act honestly, with integrity or with due skill, care and diligence. Other regimes adopt an approach that relies more on prescriptive rules. Whatever the approach, the principles or rules that govern behaviour should be unambiguous as to what is and is not acceptable behaviour and the consequences for engaging in improper conduct. Principles and rules can be supported by regulatory guidance. Enforcement actions serve to amplify the scope and meaning of rules and principles.

## Transparency laws and procedures

25. The value of a well-developed legal and regulatory framework and a robust enforcement programme is diminished if industry participants are unaware of it or of the possible consequences of non-compliance with its requirements. As a starting point and in order to play by the rules, individuals and entities should know what the rules are and the possible consequences of non-compliance.
26. Knowledge and understanding of the law will, of itself, result in compliance with the law for the majority of the population, who are law abiding citizens. The failure to comply with obligations may sometimes arise due to insufficient awareness of the law and its application. The regulated community should know: the regulatory and legal obligations that apply to them; the regulatory expectations of behaviour; and the tangible consequences for non-compliance with those obligations.
27. Transparency of laws and procedures helps develop awareness and understanding of obligations and can assist individuals and entities to comply with the laws and rules that apply to them. Transparency occurs when proposed laws and regulations are open for public consultation and when regulators publish their policies, practices, and procedures. In addition, presentation of laws and regulations in plain, easy to understand language can enhance transparency. Publication of enforcement actions, with descriptions of the misconduct and the reasons for the sanction, is an important transparency mechanism.

### EXAMPLES

Many regulators publish guidance setting out their enforcement, decision making and sanctioning processes to assist those persons who may be the subject of disciplinary proceedings and others. For example, the HK SFC publishes a pamphlet titled “Disciplinary Proceedings at a Glance”, which provides a brief overview of its disciplinary processes including criteria for determining whether to take disciplinary action, the disciplinary measures available to the HK SFC and a description of the disciplinary process. The HK SFC also publishes the “Disciplinary Fining Guideline” that shows how the HK SFC will perform its functions when imposing a fine on a regulated person by setting out the factors that the HK SFC will take into account when exercising its fining power. ASIC publishes Information Sheets on topics such as ASIC’s compulsory information gathering powers and ASIC’s approach to enforcement and Regulatory Guides, such as, administrative action against financial services providers.

ASIC has the power to designate enforceable code provisions in approved codes of conduct, a breach of which may attract civil penalties and/or other administrative enforcement action.

The Australian Government consults publicly on proposed changes to the securities and corporation's laws. ASIC seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance through public consultation papers. ASIC also consults extensively on changes to its 'market integrity rules' and notifies industry by way of online media release when it amends these rules and publishes the rules online on the ASIC website.

ASIC publishes its publicly available instruments relating to the operation of certain legal provisions either with respect to a particular individual or more generally, in the online ASIC Gazette. It also notifies industry by way of online media release when it issues a new instrument of general application.

ASIC publicises its enforcement actions in its Banned and Disqualified register online; its Enforceable Undertakings Register; and in the online ASIC Gazette.

The British Columbia Securities Commission (BCSC)'s website has numerous public materials which the public can use. Among them is a document titled "Your Guide to Settlements and Hearings" that sets forth, in plain language, what individuals can expect at hearings conducted by the BCSC.

The Federal Financial Supervisory Authority of Germany (BaFin) publishes guidelines on its fining procedures including information about deterrence, and penalty calculations. It also publishes an information sheet about its settlement procedure.

The Comissão de Valores Mobiliários of Brazil (CVM) publishes ofícios-circulares (guidance letters) which are sent to all relevant regulated entities or individuals and made publicly available on the Internet. Such letters normally contain clarifications and guidance on new rules, interpretations on the application of rules, alerts and reminders of applicable sanctions, among other features.

The Dutch Authority for the Financial Markets (AFM) together with the Dutch Central Bank publishes guidelines setting out their enforcement policy. These guidelines explain their approach to enforcement and decision making. Specifically, it explains how the AFM makes use of its powers and which factors it takes into consideration when choosing an enforcement measure. In addition, the AFM publishes enforcement outcomes on its website. Since July 2017, the AFM also publishes its fining policy, which provides guidelines for calculating the penalty amount. The enforcement policy was updated in 2020 and the fining policy was updated in 2021.

The United States Securities and Exchange Commission (US SEC) publishes its Enforcement Manual<sup>3</sup>. The Enforcement Manual contains a wide range of policies and procedures that provide guidance to the staff of the US SEC's Division of Enforcement. The public and other regulators have full access to this guide on the US SEC's website. The US SEC website also contains a wide range of information about the US SEC's enforcement outcomes such as administrative proceeding orders<sup>4</sup>, litigation releases<sup>5</sup>, and court filings<sup>6</sup>. The Division of Enforcement also publishes an annual report every year. [For example, see: <https://www.sec.gov/files/enforcement-annual-report-2020.pdf>]

The US Commodity Futures Trading Commission (US CFTC) has articulated a set of core values: "Commitment, Forward-thinking, Teamwork, and Clarity."<sup>7</sup> The Division of Enforcement has further noted that Clarity is achieved by providing market participants with greater transparency about its procedures and decision-making criteria<sup>8</sup>. In furtherance of that goal, the Division of Enforcement has publicly released its Enforcement Manual, along with other memoranda and advisories, which

3 <http://www.sec.gov/divisions/enforce/enforcementmanual.pdf>

4 <http://www.sec.gov/litigation/admin.shtml>

5 <http://www.sec.gov/litigation/litreleases.shtml>

6 See, e.g., <http://www.sec.gov/litigation/appellatebriefs.shtml>

7 [https://www.cftc.gov/media/3871/CFTC202024\\_2024StrategicPlan/download](https://www.cftc.gov/media/3871/CFTC202024_2024StrategicPlan/download)

8 [https://www.cftc.gov/media/5321/DOE\\_FY2020\\_AnnualReport\\_120120/download](https://www.cftc.gov/media/5321/DOE_FY2020_AnnualReport_120120/download)

provide further detail on certain aspects of the Enforcement programme such as the assessment of penalties and consideration of cooperation and corporate compliance programs, each of which are incorporated into the Enforcement Manual<sup>9</sup>.

SEBI publishes on its website consultation papers and invites public comments while framing/ amending new/ existing rules, regulations, circulars, etc. SEBI finalizes the proposals based on public comments received in this regard. SEBI publishes on its website all the interpretive letters/ no-action letters it issues under its Informal Guidance Scheme to various intermediaries and listed entities. Such letters generally contain guidance or interpretation of provisions of Acts/ Regulations as sought by the applicants. Further, circulars issued by SEBI, clarifying various aspects of the Regulations, are also published on the website.

### **Transparency of proceedings**

28. The ability of the public and media to observe proceedings is a discrete but important aspect of the regulatory system that can deter misconduct and one that promotes transparency and confidence in the legal, regulatory, and judicial systems. Many regulators, disciplinary tribunals and courts conduct proceedings in public. Such transparency promotes public understanding of the legal and regulatory requirements that govern behaviour in financial services regulation and is another mechanism that may influence behaviour in a positive way.

### **EXAMPLES**

ASIC may hold hearings for the purposes of the performance or exercise of any of its functions and powers under the corporation's legislation (other than for some excluded circumstances). These hearings may take place in private or be held in public. In August 2019, ASIC held two public hearings in relation to its function of providing guidance on the requirements of the laws ASIC administers. ASIC decided to use its hearing power to help it develop its regulatory guidance on certain financial sector obligations and considered a public forum to be a useful and transparent way to robustly test some of the main issues and views raised in written submissions: See further, sections 51 and 52 of the ASIC Act.

ASIC maintains a news centre on its website and regularly publishes Media Releases notifying the public about enforcement actions it causes to be initiated and the outcome, whether successful or otherwise. The Media Releases are updated with information on the progress of proceedings and outcomes including withdrawal of charges, acquittal, or successful prosecution. Links to court documents and judgments are generally included in the Media Releases. Court hearings in Australia are open to the public unless exceptional circumstances require the taking of evidence 'in camera'.

The US CFTC makes its enforcement actions public and relevant filings such as complaints, significant interim decisions, and final orders are posted on the agency's website at <https://CFTC.gov>.

### **Judicial and administrative competence**

29. The efficiency of administrative, disciplinary, and judicial processes and the quality and independence of decision making by administrative bodies, judicial tribunals and courts have a direct bearing on the credibility of a jurisdiction's financial services regulatory regime.
30. In the complex area of securities regulation, specialised knowledge can enhance the quality of judicial and administrative decision making. Specialised courts that deal specifically with securities and financial services conduct is one way to enhance the competence of decision

---

<sup>9</sup> <https://www.cftc.gov/LawRegulation/Enforcement/EnforcementManual.pdf>

makers. To the extent possible, regulators should consider engaging with the judiciary (while respecting their independence) and other authorities to keep them abreast of legislative and policy changes. Good communication between regulators and judicial authorities including, where appropriate, training for judicial authorities regarding complex financial products can also be beneficial by fostering a judiciary that understands the complexity and significance of the regulator's work.

## EXAMPLES

Some regulators organise conferences and develop training programmes to inform representatives from judicial authorities (judges and public prosecutors) about the trends and characteristics of capital market legislation and regulation. A specialised tribunal, namely the Securities Appellate Tribunal ('the Tribunal') judicially reviews the quasi-judicial orders passed by SEBI. The Tribunal consists of members with technical expertise in financial sector (including securities market).

Several regulators liaise with the judiciary and other competent authorities to develop a cadre of judges and decision makers who specialise in securities and financial services regulatory issues and to expedite proceedings involving securities and financial services activities, whilst always being mindful to protect judicial independence. In some jurisdictions, specialist divisions have been created in superior courts to deal with securities regulation actions.

### Avoiding regulatory arbitrage

31. Enforcement regimes for securities law contraventions across the globe can vary widely. Reasons for this variety are the differing institutional and procedural arrangements across jurisdictions and the diverse application of sanctions and remedies generally. IOSCO has played a role in raising standards internationally by providing a forum and mechanisms for cooperation<sup>10</sup>. Cooperation increases communication between regulators about consistency in the quality of securities regulation and ways to minimise opportunities for regulatory arbitrage.

## EXAMPLES

In March 2021, ASIC made a product intervention order imposing conditions on the issue and distribution of contracts for difference (CFDs) to retail clients. ASIC's order reduces CFD leverage available to retail clients and targets CFD product features and sales practices that amplify retail clients' CFD losses, such as providing inducements to become a client or to trade. Action was taken after ASIC found that CFDs have resulted in, and were likely to result in, significant detriment to retail clients. It also brings Australian practice into line with protections in force in comparable markets elsewhere, addressing the risk of regulatory arbitrage.

32. Enforcement of securities regulation promotes deterrence when it is perceived to be effective at addressing contraventions. Wrongdoers exploit regulatory arbitrage opportunities by committing contraventions or seeking refuge for themselves and their illicit funds in jurisdictions perceived to have weak enforcement, co-operation, and sanctioning regimes. Regulators should seek to remove opportunities for their jurisdictions to be used for regulatory arbitrage by looking for ways to reform their laws and powers, raise their own regulatory standards and enforcement effectiveness and commit to improving collaboration and cooperation with other regulators. For example, regulators may consider prohibiting conduct from its jurisdiction that causes harm, such as fraud or misleading investors, in other jurisdictions, co-ordinating

---

<sup>10</sup> See IOSCO Principles 10 – 15 in *Objectives and Principles of Securities Regulation*, June 2010 available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf> and *IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information*, May 2002- version revised May 2012 available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD386.pdf>

investigations and sharing evidence with foreign authorities, assisting foreign authorities to serve documents commencing proceedings or other initiatives that reduce opportunities for those in their jurisdiction to engage in misconduct, or evade the consequences of engaging in misconduct, in another jurisdiction.

## Factor 2: Detecting misconduct: By having access to good information

### In brief

33. By increasing the prospects of catching and punishing wrongdoers, regulators intensify the apprehension of detection and diminish the reward for wrongdoing. Detection, as a mechanism of deterrence, seeks to ensure that those who are involved in misconduct, or are contemplating involvement, have a strong expectation that the conduct will be discovered, investigated, and sanctioned. Detection mechanisms can be more effective when regulators are linked in and create systems that facilitate the sharing of intelligence and information by the regulated population and the public and between regulators, both at national and international level.
34. Misconduct can be deterred when regulators:
- a.) have robust market surveillance programmes and invest in technologies and resources to enhance surveillance commensurate with the nature, scale and complexity of markets;
  - b.) establish mechanisms to conduct surveillance of or receive information arising from inter-exchange and cross border transactions and contracts;
  - c.) co-operate and proactively share information with other international securities regulators;
  - d.) develop functions to receive complaints and tips from the public;
  - e.) create clear and effective pathways for examiners and other supervisory staff to report misconduct to enforcement;
  - f.) oblige and influence gatekeepers to report misconduct to the appropriate authorities;
  - g.) develop programmes to encourage whistleblowing to regulators; and
  - h.) work with self-regulatory financial industry organisations (SROs) and trade bodies to achieve timely provision of information about suspected misconduct or relevant trends in the industry.

### In detail

#### Market Surveillance

35. Market surveillance is a central feature of many regulatory and enforcement programmes. Its primary aim is to detect misconduct, manipulation, and other abusive practices.
36. Many regulators are now equipped with the technology, resources, and competence to conduct surveillance on a real-time or near real-time basis. However, regulation of algorithmic trading and other complex trading techniques is proving challenging even for mature jurisdictions. Regulators should consider how investing in technologies and resources, commensurate with the nature, scale, and complexity of the markets they regulate can enhance deterrence.
37. Regulators should consider whether their technologies are adequate for the task. For example, they could employ innovative tools including the latest market monitoring and alerting software, to detect market misconduct and take immediate action when required.

#### EXAMPLES

Many regulators make use of market surveillance and cyber surveillance technologies and teams to monitor the markets and the internet for early warning signs of misconduct, so that they can intervene rapidly in the interest of investors. For example, the Québec Autorité des Marchés

Financiers (QAMF) recently developed an initiative to monitor issuers who are quoted on the United States Over the Counter markets to ensure that selected issuers are not used in conjunction with a pump and dump scheme. Throughout 2020 and 2021, the combined efforts of the various units of QAMF Enforcement and especially, the cyber surveillance specialised unit, ensured the continued deployment of an intervention- and awareness-based approach to curbing illegal activities in the crypto-asset ecosystem. Specifically, a sustained effort was made to detect and deter illegal investment offers in the area of cryptocurrency mining and educate and warn the public about non-compliant practices in the sector. The team also looked at several emerging trends in this new field of activity to ascertain the presence of unfair, abusive, or fraudulent practices.

In several jurisdictions, exchanges are required to have independent trading surveillance capacities to analyse market activities in real time using customised in-house systems and are required to refer suspicious trading activities to the regulator.

Many securities regulators have created specialist investigation and enforcement units and make significant investments in market surveillance technology. For example, the QAMF created dedicated and specialised enforcement units, i.e., the Market Manipulation and Insider Dealing division and the Economic Crimes division, to facilitate more effective and efficient investigations by tailoring its practices to deliver better outcomes.

To facilitate the supervision of trading, equity market operators are required to establish a network connection to ASIC's Integrated Market Surveillance System (IMSS) and during the course of each trading day, provide a parallel data feed consisting of all orders, trades, and quotes being processed and disseminated by the market's trading engine, and all trading session and security price and status-related messages.

The BaFin has developed specialised sections in its securities supervision department, for securities markets analysis, as well as market manipulation and insider dealing investigations.

ASIC upgraded its Markets Assessment and Intelligence (MAI) system and enhanced its data analysis capabilities. MAI is a key business system which supports ASIC's mandated responsibilities to supervise trading on Australian licensed financial markets. This upgrade delivered more scalable and secure data storage.

The QAMF relies on a group of data analytic experts developing technological tools internally to address emerging threats and collect and analyse increasing volume of data. They have notably developed tools for the detection of insider trading and market manipulation schemes. Under the umbrella of IOSCO, they have initiated the Technology Applied to Securities Markets Enforcement Conferences (TASMEC). These conferences gather data analysts and end-user specialists from securities regulators around the world to share the most innovative tools in data analytics for the detection and prevention of financial crimes.

The QAMF team's agility in detecting fraud risks was especially important and relevant during the pandemic crisis, when scammers were more active and creative. The QAMF has access to a data repository and analytics system, designed and developed in collaboration with other Canadian Securities Administrators (CSA) jurisdictions, that enhances the QAMF's ability to detect and analyse market manipulation and insider trading. The MAP (Market Analysis Platform) system, an automated, centralised solution with the capacity to handle the complexity and scale of current market practices, will contribute to maintaining market integrity by providing advanced analytics functions for measuring, examining, and explaining potential market abuses. It will also provide the QAMF with improved market behaviour research capabilities supporting data-based regulatory

decisions.

The Financial Conduct Authority, United Kingdom (UK FCA) utilises daily transaction data from its surveillance and monitoring system (Zen), which is combined with external data feeds, to raise alerts in respect of potential market abuse<sup>11</sup>.

The China Securities Regulatory Commission (CSRC) designed and developed a data model, based on a study of the prominent attributes of insider trading, market manipulation, front running, and other market abuse contraventions, to identify market misconduct. This data model is used in conjunction with a public disclosure monitoring system that monitors news, peer information and other public disclosures about listed companies to generate intelligence for identifying market abuse contraventions.

SEBI has designed and developed a smart aggregator model called the “Early Warning System (EWS)” by integrating information available at various sources including corporate disclosures, statutory filings with the Government, information on the company’s litigations and court orders, defaults in the company/ its subsidiaries/ group/ associated companies/ entities connected to the promoters, news items, information from social media, etc. The EWS, once fully operational, would use data analytics tools to generate actionable alerts.

The Capital Markets Board of Turkey (CMB) uses sophisticated software to collect and analyse trading data. The CMB also gets data from other governmental authorities such as the national citizenship agency. The software allows searches across family members and can show conflicts of interest.

The US CFTC augments its enforcement program through both a Market Surveillance Unit and a Forensic Economists Unit. The Market Surveillance Unit, among other things, develops and utilizes sophisticated systems to analyse trade data, respond to outlying events, and identify trading or positions that warrant further enforcement inquiry. The Forensic Economists Unit conducts extensive data analysis to develop evidence for investigations into potential market manipulation, disruptive trading practices (including spoofing), and other unlawful trade-based conduct. Additionally, the US CFTC’s Division of Data (DOD) supports the Commission’s strategic objectives with respect to data and analytics through collaboration with other Divisions and Offices. Among other things, the DOD reduces data silos by joining datasets both within the Commission and from external sources for the clearest possible picture of economic and market conditions.

On a daily basis, the HK SFC monitors trading on The Stock Exchange of Hong Kong Limited and the Hong Kong Futures Exchange Limited and conducts preliminary inquiries to detect possible market manipulation or insider dealing. It also engages with firms to review how they perform their monitoring and surveillance. Through an organisation-wide Market Intelligence Programme, the HK SFC develops technologies to help it identify conduct risks in the market, including potential misconduct perpetrated by interconnected parties. Data collected from its operations and public sources is analysed to isolate patterns and connections between individuals, companies and transactions which may indicate conduct risks.

### **Cross border surveillance**

38. Inter-exchange and cross border surveillance of transactions and contracts is an increasingly important regulatory function. Regulators with access to multiple streams of information from domestic and foreign exchanges can enhance deterrence. Regulators should consider exploring ways to receive trading data from multiple exchanges and foreign regulators. They

---

11 <http://www.fca.org.uk/firms/systems-reporting/transaction-reporting/zen>

should also consider the benefits of collaborating and sharing intelligence derived from surveillance and other activities as a means of detecting and deterring misconduct. Regulators could also consider establishing arrangements for obtaining information from Financial Intelligence Units (FIUs) to supplement intelligence about transaction flows.

## EXAMPLES

Many securities regulators have created specialist investigation and enforcement units and make significant investments in market surveillance technology. For example, the QAMF created dedicated and specialised enforcement units, i.e., the Market Manipulation and Insider Dealing division and the Economic Crimes division, to facilitate more effective and efficient investigations by tailoring its practices to deliver better outcomes.

BaFin has developed specialised sections in its securities supervision department, for securities markets analysis, as well as market manipulation and insider dealing investigations.

The US CFTC requires any Foreign Board of Trade (FBOT) that provides US-based participants with direct access to its electronic trading and order matching system to register with the Commission and comply with certain conditions, which include periodic data reporting and other information-sharing requirements. With respect to so-called “linked contracts,” which settle against the price of contracts on a US exchange, a registered FBOT is further required to provide daily trade execution and audit trail data for the Commission’s Trade Surveillance System<sup>12</sup>.

The US CFTC has entered into bilateral Memoranda of Understanding (MoU) with certain foreign supervisory authorities providing for the sharing of information, solely for the supervision and oversight of specified entities required to register with the US CFTC, to ensure compliance with the relevant laws and regulations of the parties to the MoU. Although such MoUs are not intended to gather information for enforcement purposes, they provide for cooperation and information sharing to support cross-border supervision of investment services for the purpose of preserving the integrity of the market and protecting investors. Non-public information gathered under such MoUs generally may be used for purposes such as conducting investigations or taking enforcement action in accordance with the IOSCO MMoU and EMMoU, provided that both parties are signatories<sup>13</sup>.

## Reporting mechanisms for the public

39. The public can be a useful source of information and intelligence to identify misconduct. Deterrence can be enhanced when regulators have transparent, well known and easily accessible mechanisms for the public to provide tips and make complaints about suspected or actual misconduct.
40. A centralised, well-resourced, and competent tipping or complaints management function can provide valuable intelligence to regulators to identify misconduct and risks and vulnerabilities to investors and the financial system. The public will be emboldened to make complaints and provide tips if they have confidence in the integrity and responsiveness of the complaints and tips functions.

## EXAMPLES

Most regulators have electronic platforms for making and receiving complaints and tips from the public. For example, the Financial Market Authority of New Zealand (NZ FMA) provides an

<sup>12</sup> 17 C.F.R. § 48.1 et seq.

<sup>13</sup> See, e.g., <https://www.cftc.gov/PressRoom/PressReleases/8321-20>; <https://www.cftc.gov/PressRoom/PressReleases/8289-20>

anonymous complaints portal on its website. The portal offers strong anonymity and does not record or retain the ISP addresses of informants.

The CMB complaints system offers the option for complainants to disclose their identity or remain anonymous.

Also, the Italian Commissione Nazionale per le Società e la Borsa (CONSOB) allows complaints to be submitted anonymously, including through a portal on its website.

The ASIC Regulatory Portal improves how stakeholders interact with ASIC. A new suite of regulatory transactions was added to the portal in 2019–20, including breach reporting for Australian financial services (AFS) licensees and registered auditors, and insolvency statutory reporting.

The Market Entity Compliance System (MECS) is an online regulatory compliance portal that provides market entities with tools and information to assist them in complying with several of their regulatory obligations. The portal is available to market participants, market operators, clearing and settlement facility operators and derivative trade repository operators

ASIC provides an online form where members of the public and potential whistleblowers can report their concerns or potential misconduct. ASIC will not reveal the identity or the contents of the report to others unless required or authorised by the law to do so.

Since 2019, the AFM informs the public every six months about signals it receives, and what action the AFM takes with regard to these signals (without disclosing confidential information). To that end, the AFM uses both traditional media and social media (Twitter) in order to maximise media exposure.

SEBI has established an online investor grievance redressal system (viz. SEBI Complaints Redress System - 'SCORES' in short). Information provided by any person under the categories of price/ market manipulation, accounting manipulation and insider trading, in the SCORES system, are treated as market intelligence.

SEBI has initiated enforcement action in several cases wherein money was solicited from the public without following the legal provisions for public issue based on complaints received from aggrieved investors.

The US CFTC created the Office of Customer Education and Outreach (OCEO), which is dedicated to helping customers prevent and protect themselves from fraud or violations of the Commodity Exchange Act. Among other things, OCEO encourages and facilitates the inflow of information from the public about potential misconduct. Through traditional and social media outreach, as well as direct engagement with industry and individual customers, OCEO educates customers about how to report fraud, other potential violations, or suspicious activities to the US CFTC. The US CFTC can receive complaints online at [cftc.gov/complaint](https://cftc.gov/complaint) and via a dedicated complaint hotline telephone number also available on [cftc.gov](https://cftc.gov). Members of the public may also seek to report potential misconduct in connection with the US CFTC's whistleblower program, which provides monetary incentives to individuals who report possible violations of the Commodity Exchange Act that lead to a successful enforcement action, as well as privacy, confidentiality, and anti-retaliation protections for whistleblowers<sup>14</sup>. Additionally, through the reparations program, customers may directly file complaints against futures industry professionals registered with the US CFTC at [cftc.gov/complaint](https://cftc.gov/complaint).

The HK SFC sets up a section titled "*Have you seen these people?*" in its website. This section

---

<sup>14</sup> <https://www.whistleblower.gov>

contains details of individuals who are the subject of arrest warrants or whom it believes have important information that may assist in other enforcement inquiries. The HK SFC encourages the public to help it find individuals who are sought in relation to enforcement inquiries but cannot be traced. Locating and speaking to people who have relevant information is an important part of its investigation work.

### **Intra agency information flows**

41. The flow of information within a regulatory agency is as critical as the flow of information between regulatory and enforcement agencies. Specialist divisions, including supervision and surveillance programmes, frequently identify misconduct at an early stage. Deterrence can be enhanced when regulators provide pathways for examiners and other supervisory staff to report misconduct to enforcement. The timely flow of information from supervisory and surveillance programmes to enforcement can enable regulators to intervene and deter misconduct before it becomes widespread.

### **Gatekeepers**

42. Jurisdictions can enhance deterrence by giving regulators ways to acquire information from gatekeepers, such as through compulsory reporting requirements enshrined in legislation. Compliance officers, trustees, auditors, credit rating agencies, issuers and their managers/directors, sponsors and professional advisers are important sources of information. Regulatory obligations placed on those persons and entities to make disclosures about any activity that might constitute a contravention of laws, regulations or policies can serve to promote deterrence. Regulators can consider ways to enhance the quality and timelines of reporting, e.g., by holding gatekeepers accountable for their acts and omissions.

### **EXAMPLES**

In many jurisdictions regulated entities are routinely required to provide Suspicious Transaction Reports to the regulator in the event the entity becomes aware of circumstances that might constitute a suspicious transaction that contravenes anti-money laundering laws, or which might constitute informed trading ahead of an announcement.

Many jurisdictions require licensed entities, their auditors, company receivers and liquidators to disclose, to the regulator, any information which might show an illegal act, or a failure to comply with legal obligations by a regulated person or its officers or a public company and its officers.

In South Korea, each financial institution and electronic financial business operator is required to report to the Financial Services Commission (SK FSC) and the Governor of the Financial Supervisory Service (SK FSS) any IT incidents that result in, for example, suspensions or delays in IT services to consumers or markets caused by cyber-attacks, manipulation of computer data, hacking or systems failure.

The US SEC's *Operation Broken Gate* focuses on holding accountable gatekeepers who fail to carry out their duties and responsibilities in a manner consistent with professional standards. Under this initiative, auditors, attorneys, and other gatekeepers, who have special duties and responsibilities to safeguard the interests of investors, have been held accountable.

In the US, the Commodity Exchange Act and US CFTC Regulations require certain categories of registrants to appoint a Chief Compliance Officer (CCO) and further require the CCO to submit an annual compliance report ("CCO Annual Report") identifying, among other things, areas for improvement and material non-compliance issues. The US CFTC has held CCOs, other senior

executives and board members, including Chairmen, liable for misconduct that occurs under their watch, by charging such individuals with supervisory failures or holding them vicariously liable, as controlling persons, for the actions of their employees and agents. Additionally, in an effort to promote a strong culture of compliance in the industry the Division of Enforcement has issued guidance clarifying how the effectiveness of a compliance program will be evaluated in the enforcement context, focusing on whether it is reasonably designed and implemented to (i) prevent the underlying misconduct at issue; (ii) detect the misconduct; and (iii) remediate the misconduct<sup>15</sup>.

SEBI Regulations mandate Compliance Officer appointed by the market infrastructure institutions and intermediaries to promptly and independently report, to SEBI, information pertaining to non-compliance of securities laws. Further, SEBI, has, under the SEBI (Prohibition of Insider Trading) Regulations, 2015, mandated that every organization should have a financially literate Compliance Officer who shall be responsible for compliance of policies, procedures, maintenance of records, monitoring adherence to the rules for the preservation of unpublished price sensitive information, monitoring of trades and the implementation of the codes of conduct specified in these regulations. Also, in cases of financial misstatements, SEBI has held statutory auditors accountable under the SEBI Act and Regulations framed thereunder.

## Whistleblowers

43. Whistleblowers are a useful source of information and intelligence. Reporting can be enhanced when jurisdictions provide legal protection to whistleblowers to prevent them from being adversely impacted or prejudiced as a result of providing information.

### EXAMPLES

A number of jurisdictions have legislation that affords confidentiality and legal protection to whistleblowers that make it unlawful for action to be taken by their employers for their whistleblowing.

For example, the New Zealand Protected Disclosures Act provides protection to employees who make complaints to authorities. Confidentiality is also afforded to informants through other legislation including the Evidence Act and Securities Act. In 2012, the New Zealand courts recognised the importance of informants and, on the NZ FMA's application, prevented the disclosure of a whistleblower's statement and the identity of an informant in a Securities Act investigation.

The US Commodity Exchange Act similarly prohibits, with limited exceptions, the disclosure of information by the Commission that could reasonably be expected to reveal the identity of a whistleblower and contains anti-retaliation provisions which are enforceable via a private action or, under certain conditions, through an enforcement action brought by the US CFTC<sup>16</sup>.

From 1 July 2019, the Australian Whistleblower Protection regime has been expanded to provide greater protections for whistleblowers who report misconduct about companies and company officers and employees. Under that legislation a person who makes a "qualifying disclosure" cannot be subject to any civil, criminal, or administrative liability (including disciplinary action) for making the disclosure. The Australian Corporations Act requires public companies, large proprietary companies, and corporate trustees of superannuation entities regulated by APRA to have a Whistleblower policy. The policy must set out how those companies will support and protect whistleblowers and handle their disclosures.

---

<sup>15</sup> <https://www.cftc.gov/media/4626/EnfGuidanceEvaluatingCompliancePrograms>

<sup>16</sup> 7 U.S.C. § 26; 17 C.F.R § 165

The Australian Corporations Act 2001 provides certain protections for officers, employees or contractors of a company who make a report on that company.

- Whistleblowers can report misconduct through ASIC's online form.
- ASIC released an Immunity Policy in 2021 for whistleblowers who could be liable for criminal or civil action in relation to any role they played in the conduct that they are reporting (contravening Part 7.10 of the Corporations Act).
- In November 2019, ASIC released Regulatory Guide 270 Whistleblower policies (RG 270) to assist these companies to meet their obligations under the law to have a Whistleblower policy.

The US CFTC are authorised to reward eligible individuals who come forward with high-quality original information that leads to an enforcement action in which over \$1 million in sanctions is ordered. The range for awards is between 10% and 30% of the money collected<sup>17</sup>. The US SEC and US CFTC have each established an Office of the Whistleblower to administer their respective programmes<sup>18</sup>.

European Union (EU) Regulation No 596/2014 introduces a framework for whistleblowers in the Market Abuse regime applicable in the European Economic Area so that adequate arrangements are in place to enable whistleblowers to alert competent authorities in EU Member States to possible infringements of market abuse regulations and to protect them from retaliation. The regulation allows Member States to provide financial incentives for those persons who offer relevant information about potential infringements of market abuse regulations.

Other Union acts in the area of financial services, including among other Directive 2014/65/EU on markets in financial instruments, Directive 2009/65/EC on UCITS and Regulation (EU) 2017/1129 on prospectuses, set out similar frameworks on whistleblowing.

SEBI has put in place Informant Protection guidelines under which any individual can provide information pertaining to violation of Insider Trading laws to SEBI in a simple and readily accessible format. The identity of the Informant is not disclosed publicly and there are provisions for suitably rewarding the Informant. Listed companies have also been mandated under the Insider Trading laws to have a Code of Conduct that provides for suitable protection against termination, suspension or any other adverse action against any employee who submits information to SEBI and to have an effective whistleblower policy and mechanism so that stakeholders, including individual employees and their representative bodies, to communicate concerns about illegal or unethical practices.

SEBI (Settlement Proceedings) Regulations, 2018 allows for a mechanism of settlement with confidentiality, whereby, SEBI provides the benefit of confidentiality to an applicant in exchange for admitting to the charges for the limited purpose of settlement of certain proceedings and agreeing to provide substantial assistance in any investigation/ examination against any other person.

The Ontario Securities Commission (OSC) has an Office of the Whistleblower. The OSC's Whistleblower Program accepts tips on possible violations of Ontario securities law, offers protections for individuals who come forward, as well as a reward of up to CAD \$5 million for tips that lead to enforcement action. It is recognized that whistleblowers can expose complex securities misconduct that may not otherwise be exposed, and which allows for more timely enforcement action. Certain protections are set forth in Ontario's Securities Act which are designed to protect whistleblowers against reprisals.

---

17 Section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act available at <https://www.sec.gov/mwgq-internal/de5fs23hu73ds/progress?id=JATaK1jCrW> mandated that the US SEC establish a Whistleblower programme to make significant monetary rewards to eligible individuals who voluntarily provide original information that leads to successful Commission enforcement actions.

18 See <http://www.sec.gov/whistleblower> and <https://www.whistleblower.gov>

## Targeted programmes

44. The unique characteristics of each market, including its type, size, and maturity, will determine the characteristics of surveillance programmes necessary to detect and disrupt misconduct. For example, financial reporting and audit programmes are a common feature of most mature and some emerging jurisdictions.
45. Commodity, equity, financial and other specialised markets require specialised surveillance skills and technologies. To the extent possible, regulators should consider dedicating resources to cutting edge tools and infrastructure to help them fulfil their mandates.

### EXAMPLES

The US SEC launched the Centre for Risk and Quantitative Analytics, which helps it develop technologies to analyse trading and other types of data available from a wide variety of venues<sup>19</sup>.

The US CFTC engaged in a multi-year project to strengthen its data analytics capability to enhance the ability to identify, in the trading data, forms of misconduct that might otherwise have been undetectable. The agency obtains comprehensive trade data directly from exchanges approximately one day post-transaction. An analytics team comprised of enforcement lawyers, ex-traders, and software engineers employs these new tools to rapidly analyse trades and identify patterns of suspicious activity. Using these new tools, the agency is able to review the electronic order book and look across markets, which has enabled the US CFTC to not only spot misconduct, such as spoofing and wash trading, but also to uncover false and misleading statements.

In July 2022, the CFTC launched the Office of Technology Innovation (OTI), which serves as the CFTC's financial technology innovation hub, driving change and enhancing knowledge through innovation, consulting/collaboration, and education. OTI fosters innovation in CFTC's regulatory oversight and mission critical functions by supporting the operating divisions and the Commission's participation in domestic and international coordination. OTI regularly advocates for the advancement of responsible innovation, industry collaborations, and public outreach and education.<sup>20</sup>

ASIC's financial reporting surveillance programme aims to improve the quality of financial reporting. ASIC reviews the annual and interim financial reports of a selection of listed companies and other significant entities, to monitor compliance with the Corporations Act and Australian Accounting Standards.

Auditor surveillances generally arise through complaints from the public to ASIC or through media reports and intelligence from other areas of ASIC, for example the financial reporting surveillance programme, where queries are raised about the performance of an auditor or the nature of the audit report.

ASIC's audit inspection programme reviews compliance with audit quality and auditor independence requirements. Registered company auditors and firms are required to comply with the Corporations Act and follow all auditing standards and other requirements that are relevant to each engagement.

## Self-regulatory and industry supervisory groups

46. A feature of securities enforcement, particularly in mature jurisdictions, is the widespread use

---

<sup>19</sup> SEC Announces Enforcement Initiatives to Combat Financial Reporting and Microcap Fraud and Enhance Risk Analysis, Securities and Exchange Commission, 2 July 2013, available at <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171624975>

<sup>20</sup> <https://www.cftc.gov/OTI/index.htm>

of SROs to monitor parts of the financial services industry. SROs play an increasingly important role in guiding the behaviour of industry participants. Deterrence arising from enforcement activities is supported when SROs and other industry organisations collaborate with the regulator. Conversely, an SRO without robust and committed regulatory infrastructure can undermine a regulator's efforts to promote credible deterrence. Regulators should consider having regular dialogue with SROs, and/or inspections of SROs, to ensure they fulfil their regulatory mandates and provide information, on a timely basis, about suspected misconduct. Regulators could also encourage SROs to strengthen their governance and the quality of their compliance and risk management arrangements in ways that would enhance deterrence.

47. Securities laws and regulations that require regulated entities to monitor compliance within their own institutions can assist in the identification of misconduct. Regulated entities are likely to be well-placed to know where risks exist for their employees and/or clients to engage in misconduct. Laws and rules that require entities to construct and monitor controls systems can also contribute to deterring misconduct. Moreover, holding managers accountable for the proper functioning of compliance systems can bolster a regulator's ability to send the message that contraventions will be detected. If managers can be sanctioned for failing to detect and prevent misconduct by their direct reports, this should incentivise them to prevent such misconduct.

## EXAMPLES

The Securities and Exchange Surveillance Commission of Japan (SESC) has been working with SROs, such as securities exchanges and the Japan Securities Dealers Association, to ensure that the SROs are actively taking steps to prevent fraudsters from entering the markets.

German securities exchanges are self-regulatory in that they are required to have independent trading surveillance offices that work together closely with and send reports directly to BaFin's securities monitoring department.

The US SEC works with SROs, such as the Financial Industry Regulatory Authority, (FINRA) which has developed a programme called the Securities Observation, News, Analysis and Regulation system that flags unusual price and volume movements in traded securities and identifies potential insider trading and fraud against investors<sup>21</sup>.

Memoranda of Understanding between respectively the US SEC and the US CFTC with the Financial Crime Enforcement Network (FinCEN) provides FinCEN with detailed information on a quarterly basis regarding the anti-money laundering and enforcement activities of the US SEC, the US CFTC and SROs. In turn, under the agreements, FinCEN provides assistance and analytical reports to the US SEC<sup>22</sup> and the US CFTC

US securities laws authorise the US SEC to sanction brokers and dealers that fail reasonably to supervise persons associated with regulated entities who commit contraventions of the US securities laws<sup>23</sup>.

The US CFTC regulations require registrants to diligently supervise their officers, agents and employees<sup>24</sup>. The Commodity Exchange Act also provides that principals may be held liable for violations by their agents<sup>25</sup> and individuals found to be "controlling persons" may be held liable for

---

<sup>21</sup> See *FINRA Retooling Market Surveillance to Catch Abuses*, Bloomberg News, 18 December 2010 available at <http://www.bloomberg.com/news/2010-12-17/finra-plans-to-improve-surveillance-to-catch-insider-trading.html>

<sup>22</sup> *SEC and FinCEN Sign Information Sharing Agreement*, 21 December 2006, available at [http://www.fincen.gov/news\\_room/](http://www.fincen.gov/news_room/)

<sup>23</sup> See Section 15(b)(4)(E) of the Securities Exchange Act of 1934 available at <https://www.sec.gov/mwg-internal/>

<sup>24</sup> 17 C.F.R. § 166.3

<sup>25</sup> 7 U.S.C. § 2(a)(1)(B)

violations by those they control<sup>26</sup>. The US CFTC Division of Enforcement has taken further steps to encourage robust corporate compliance programs and has issued guidance which outlines factors the Division considers when evaluating compliance programs in connection with enforcement matters<sup>27</sup>.

The US SEC has developed under its Quantitative Analytics Unit a National Exam Analytics Tool (NEAT). With NEAT, US SEC examiners are able to access and systematically analyse extremely large amounts of trading data from entities in a fraction of the time that it had taken in the past<sup>28</sup>.

The US CFTC routinely participates in cooperative enforcement activities with federal and state authorities, both civil and criminal, as well as regulated entities such as derivatives exchanges and swap execution facilities as well as with the National Futures Association in various ways. This includes, a robust referral process, information sharing, providing technical assistance and subject matter training, and at times, coordinating on parallel investigations or enforcement actions. Additionally, through coordination and cooperation with SROs covering entities or products that may be outside the scope of the US CFTC's jurisdiction, such as FINRA, the US CFTC is better able to engage in cross-market surveillance and enforcement.

---

<sup>26</sup> 7 U.S.C. § 13c(b)

<sup>27</sup> <https://www.cftc.gov/media/4626/EnfGuidanceEvaluatingCompliancePrograms091020/>

<sup>28</sup> Chair Mary Jo White, *The SEC in 2014*, 27 January 2014, available at <http://www.sec.gov/News/Speech/Detail/Speech/1370540677500>

### Factor 3: Co-operation and collaboration to eliminate wrongdoer safe havens

#### In brief

48. Deterrence against misconduct is enhanced by securities regulators working together with criminal authorities and other domestic and international agencies to:
- a.) share information (both public and non-public); and
  - b.) strengthen their detection, investigation, prosecution, and sanctioning capabilities in response to wrongdoing.
49. The incentives for misconduct are reduced when wrongdoers become aware that regulators and agencies are working together to remove safe havens, disgorge the proceeds of unlawful activity and prosecute offenders. Domestic and international co-operation arrangements, such as the IOSCO Multilateral Memorandum of Understanding (MMoU)<sup>29</sup> and Enhanced MMoU (EMMoU)<sup>30</sup>, can assist in deterring misconduct because they make it more difficult for wrongdoers to operate from a foreign jurisdiction.
50. Misconduct can be deterred when regulators:
- a.) co-operate with domestic and international industry bodies, SROs, other regulators, enforcement and prosecution authorities, administrative, civil, criminal judicial decision makers (where permitted and as appropriate) and governments to enhance the effectiveness of enforcement;
  - b.) take the necessary measures to satisfy the preconditions for signing the IOSCO MMoU and EMMoU, including the removal of legal obstacles for the sharing of information and co-operation;
  - c.) ensure that restrictive conditions are not placed on co-operative or collaborative efforts;
  - d.) promote their government's ratification of international conventions, treaties and agreements that enhance the effectiveness of domestic enforcement programmes;
  - e.) consider other formal channels for the sharing of information, such as the traditional gateways in a treaty for mutual legal assistance and agreements of mutual understanding;
  - f.) share information about misconduct, and emerging and existing enforcement risks;
  - g.) have an efficient centralised process for the prioritisation and timely execution of information requests from other regulators; and
  - h.) participate in domestic and international fora to enhance the capacity and effectiveness of enforcement.

#### In detail

51. Multilateral approaches to enforcement are producing outcomes that could not be achieved through unilateral action alone. Collaborative enforcement efforts are now adopted to counter global misconduct. Wrongdoers across multiple jurisdictions are increasingly scrutinised and held accountable by coordinated investigatory and enforcement efforts.
52. Regulators should consider all opportunities to ensure effective domestic and global

---

<sup>29</sup> <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD386.pdf>

<sup>30</sup> <https://www.iosco.org/about/pdf/Text-of-the-EMMoU.pdf>

cooperation. Regulatory enforcement tools should:

- a.) provide a basis for the exchange of information, and the sharing of intelligence on emerging and existing risks; and
- b.) facilitate (where authorised) the exercise of enforcement powers, such as conducting compulsory interviews or securing freezing orders.

53. In addition, informal networks among regulators are helpful; particularly for the early identification of, and a quick response to, issues.

### **International**

54. Conducting cross border investigations is challenging and can be made more difficult by the legal and cultural differences between jurisdictions.

55. International arrangements, such as the IOSCO MMoU and EMMoU, may assist in deterring wrongdoers by facilitating information sharing and co-operation that may ultimately lead to the prosecution of illegal conduct and the disgorgement of illicit profits.

56. Although there is presently strong co-operation between many securities regulators, especially as facilitated by the IOSCO MMoU and EMMoU, all jurisdictions can look for ways to improve cooperation, and, as a consequence, deterrence. For instance, regulators should consider reducing restrictions on their ability to share information with domestic and foreign counterparts. IOSCO has significantly facilitated the sharing of information by encouraging those securities regulators who are not signatories to the MMoU and EMMoU to amend their legal frameworks and become signatories. IOSCO has also urged regulators to commit to the spirit and letter of the IOSCO Principles and to the collaborative arrangements espoused in the MMoU and EMMoU, which are based on the concept of providing the fullest assistance permissible.

### **EXAMPLES**

Many securities regulators have specialised international units that are charged with liaising with foreign authorities, both civil and criminal, and that handle incoming and outgoing enforcement-related requests, such as those made under the IOSCO MMoU and EMMoU.

In the course of an investigation ASIC had requested assistance under the IOSCO MMOU, from a foreign regulator to obtain documents from an entity in that jurisdiction. The Chief Executive Officer of the foreign entity challenged ASIC's request for production of information and documents and also sought production of material obtained by ASIC from the requested authority, including the MMOU request for assistance. ASIC defended the challenges to the exercise of its powers and also resisted the production of information relating to its MMOU request and exchange of correspondence with the requested authority on the grounds that public interest immunity applied to maintaining the confidentiality of the documents. ASIC was successful on all grounds.

57. In addition to becoming signatories to the IOSCO MMoU and EMMoU, jurisdictions should consider how other international agreements might enhance the effectiveness of enforcement. Regulators should consider consulting with relevant authorities who have the power to enter into:

- a.) agreements for mutual assistance that provide a legal basis for transmitting evidence between jurisdictions for use in proceedings;
- b.) arrangements with FIUs to trace and track transactions and the proceeds of crime; and,

- c.) bilateral agreements of mutual cooperation and understanding between jurisdictions that provide cooperation beyond scope of the IOSCO MMoU and EMMoU.
58. Authorities in some jurisdictions have the power to prosecute contraventions of securities laws, such as insider dealing, criminally. However, the powerful deterrent effect of potential criminal prosecution can be undermined if suspects are able to simply leave the jurisdiction to avoid prosecution, penalty, or arrest. International cooperation is essential in order to bring such suspects to justice.
59. Securities regulators who have criminal jurisdiction should also consider how they can best assist overseas counterparts to extradite individuals and freeze and repatriate assets. This is likely to involve liaison with FIUs and domestic criminal authorities and include arrangements that provide information about individuals, their accounts, investments and assets that can be readily shared with domestic and foreign authorities.
60. Jurisdictions should consider whether:
- a.) there is an adequate legal framework for the extradition of individuals and for the freezing and repatriation of assets;
  - b.) securities and financial services law contraventions should be extraditable offences;
  - c.) there are transparent and efficient processes for responding to extradition requests, restraining conduct and, where applicable, freezing, confiscating, and repatriating assets; and
  - d.) the process and requirements for extradition, restraining of conduct, and the freezing, confiscation and repatriation of assets are unduly restrictive or protracted.

## EXAMPLES

The UK Financial Services Authority (the UK FCA's predecessor) have been successful in the extradition, conviction, and incarceration of individuals on criminal charges. Further, an overseas regulator can make a direct application to the UK courts to freeze assets in cases concerning claims of compensation, disgorgement, or restitution. The UK High Court will grant a freezing order, "In all cases in which it appears to the court to be just and convenient to do so".

The UK FCA has an established gateway under the domestic legislation for disclosure, for the purpose of criminal proceedings and investigations. The gateway is reinforced under the Memorandum of Understanding (MoU) with law enforcement bodies across the UK providing for bilateral and multilateral engagement on criminal issues. The FCA is a member of the FIN NET, a domestic and international working group for the exchange of intelligence and information sharing across regulatory and law enforcement bodies.

The European Arrest Warrant (EAW) replaces extradition arrangements between individual EU member states. Under the rules of the EAW, an EU member state cannot refuse to surrender its citizen to another EU member state where that citizen has committed, or is suspected of having committed, a serious crime (including, for example, fraud and money laundering).

ASIC has also been successful in the extradition, conviction, and incarceration of individuals on criminal charges. An Australian company director was extradited from a South-East Asian jurisdiction in September 2017 following collaboration with the Commonwealth Director of Public Prosecutions and Australian Federal Police. The director was charged in Australia with 16 counts of using his position as a director dishonestly with the intention of gaining an advantage for himself

or others and two counts of giving false or misleading information to the Australian Securities Exchange. The extradition was done with the assistance and cooperation of the various authorities in the foreign jurisdiction.

61. In addition to the cooperation arrangements under the MMoU and EMMoU, regulators should consider having internal protocols for collaborating with other regulatory agencies. The IOSCO Joint and Parallel Investigations Guide<sup>31</sup> is a helpful template. The protocols may contain practical procedures such as establishing regulatory colleges and other information-sharing mechanisms to share information about actions, timeframes, prosecutions, and settlements.
62. When conducting a joint or parallel investigation, regulators should take into account differences between jurisdictions. Cooperation between the authorities in both jurisdictions will be critical in effectively progressing investigation of the misconduct and taking successful enforcement action.
63. Regulators can also:
  - a.) share know-how;
  - b.) inform relevant stakeholders, including legislators and international standard-setting bodies, of emerging and existing securities related risks;
  - c.) advise as to whether national and international approaches to the enforcement of securities law adequately mitigate the risks; and
  - d.) provide feedback as to the efficacy of the collective response.

## EXAMPLES

The OSC, like some of its Canadian counterparts, has the ability to freeze assets, on an *ex parte* basis, on behalf of another regulator.

The Dubai Financial Services Authority (DFSA) has used its executive powers to freeze assets<sup>32</sup> on behalf of another regulator<sup>33</sup> after the DFSA informed that regulator that assets had entered its jurisdiction which were suspected of being the proceeds of a Ponzi scheme in that jurisdiction. Following this action by the DFSA, the overseas regulator applied to the DIFC Courts for formal orders freezing the assets and was successful in obtaining those orders.

The members of IOSCO's Committee 4 on Enforcement and the Exchange of Information regularly share information on significant cases, innovative investigation and enforcement practices and emerging risks to investors.

European securities regulators that are members of ESMA's Market Integrity Standing Committee regularly exchange views on the application of European and national market integrity laws in the respective states.

## Domestic

64. IOSCO focuses on international co-operation between regulators. However, regulators should

<sup>31</sup> Non-public Report of IOSCO Committee 4 for Enforcement and the Exchange of Information, (IOSCO member's only webpage).

<sup>32</sup> Article 76 - Restriction on Dealing with Property of the Regulatory Law, DIFC Law No 1 of 2004., available at [http://dfsa.complinet.com/net\\_file\\_store/new\\_rulebooks/d/f/DFSA1547\\_7446\\_VER170.pdf](http://dfsa.complinet.com/net_file_store/new_rulebooks/d/f/DFSA1547_7446_VER170.pdf)

<sup>33</sup> Article 39 - Exercise of Powers on behalf of other Regulators, of the Regulatory Law, DIFC Law No 1, of 2004 available at [http://dfsa.complinet.com/net\\_file\\_store/new\\_rulebooks/d/f/DFSA1547\\_7446\\_VER170.pdf](http://dfsa.complinet.com/net_file_store/new_rulebooks/d/f/DFSA1547_7446_VER170.pdf)

consider how domestic co-operation arrangements can enhance deterrence. Effective collaboration between domestic authorities can lead to better enforcement outcomes that are likely to deter misconduct in the future.

65. Such co-operation could include:

- a.) arrangements that facilitate information sharing and co-operation between regulators, financial intelligence units, the police, prosecution and other appropriate authorities or agencies;
- b.) arrangements to develop the enforcement and regulatory capabilities of relevant authorities; and
- c.) appropriate collaboration with industry and SROs to understand emerging risks and deal with breaches of industry and regulatory standards.

## EXAMPLES

Several jurisdictions have co-operation agreements between regulators and other enforcement agencies under which intelligence and resources are shared. For example, the US SEC has entered into a MoU with the US Federal Bureau of Investigation (FBI) to embed FBI agents within the US SEC's Office of Market Intelligence. There is also a MoU that helps ensure continued coordination and information sharing between the two agencies. Additionally, in 2020 the SEC and Department of Justice Antitrust Division signed an interagency MoU to foster cooperation and communication between the agencies with the aim of enhancing competition in the securities industry.

A formal mechanism is in place in India wherein frauds are reported by banks against entities/corporates and these reports are shared thereafter, on an ongoing basis, with SEBI by the Central Economic Intelligence Bureau. SEBI has also signed bilateral Memorandum of Understanding with other Organisations/ Regulators of India working in the area of financial sectors, namely the Ministry of Corporate Affairs (MCA) and the Central Board of Direct Taxes (CBDT) for sharing of data and information.

In a monthly meeting the AFM, the Fiscal Information and Investigation Service and the Dutch Public Prosecutor discuss the method of enforcement in investigations that lead to the finding of contraventions of the law. The aim of this meeting is to prevent the duplication of sanctions. Besides this monthly meeting, those parties also discuss in a regular "Signal meeting" signals regarding possible contraventions of financial and criminal law in the financial sector. They also contact each other on an ad hoc basis regarding possible contraventions of financial and criminal laws.

The AFM is one of the participants of Dutch Financial Expertise Centre (FEC). The FEC is a partnership of authorities with supervisory, investigative, and law-enforcement functions in the financial sector and was founded to boost the integrity of this sector. By participating in the FEC, AFM increases its information position and knowledge. The AFM regularly receives information from its FEC partners. In certain circumstances, FEC partners can also establish a FEC data room so as to allow for further discussions between FEC partners and the exchange of information.

The CVM has co-operation agreements with other enforcement agencies under which intelligence and resources are shared. For example, the CVM has entered into MoUs with the Federal Police and the Federal Prosecutor's Office in order to enable higher agility and effectiveness in prevention, diligence and suppression of harmful practices in the securities market. This objective has been achieved through: (i) exchange of information, documents and technical papers related

to securities market regulation and supervision; (ii) technical and scientific cooperation through studies and research and; (iii) appropriate legal measures to defend securities market interests and its respective investors.

The Comisión Nacional Bancaria y de Valores of Mexico (CNBV) has the power to coordinate with other local financial authorities (i.e., Banking and Insurance Commission, Pension Funds Commission, Protection of the Users of Financial Services, Central Bank, and Federal Deposit Insurance Institute) concerning joint inspection visits, without prejudice to the independence of investigations and inspections conducted by the individual financial authorities. Moreover, when any local financial authority detects a potential contravention with an entity under the supervision of another authority (e.g., the CNBV), it will give immediate notice to the other authority, so potential or actual wrongdoing may be detected in a timely manner and enforcement actions can be triggered immediately on a joint or individual agency basis.

The SK FSC and the SKFSS have measures to detect cyber-attacks through the Electronic Financial Emergency System and have acted swiftly in response to cyber threats by running cyber-attack countermeasure systems at banks and at the Korea Financial Telecommunications and Clearing Institute (KFTC) to minimise any potential damage. An Emergency Countermeasure Task Force has been formed between the FSC/ FSS, and the KFTC to closely monitor any suspicious activities or signs of further attacks. Banks and financial companies are alerted to such attacks and are directed to run 24-hour emergency monitoring surveillance.

In Canada, the law operates so that when a securities regulatory authority in one province issues a decision or enters into an agreement with a person imposing sanctions, conditions, restrictions or requirements, it will automatically apply, without notice or hearing, in the other Canadian provinces (except Ontario). The decision or agreement has the effect as if it were made by these other provinces' regulatory bodies. If the decision or agreement is amended or revoked, the amendment or revocation will also automatically apply.

The QAMF has a structured partnership with police forces and criminal prosecutors. The partnership fosters efficiency, better allocation of resources and better results. There are many situations where a contravention may be sanctioned under both the Securities Act and the Criminal Code and, therefore, both prosecutors and regulators have jurisdiction. These partnerships avoid duplication of work, legal and operational gaps and overlapping proceedings. The cooperation also has the effect of bringing expertise together. The police have criminal investigation expertise and tools (such as wiretaps) but do not necessarily have team's economic crime expertise. When the initial case assessment leads the QAMF to believe that the matter can be subject to a criminal investigation (and that, for example, wiretap evidence may be required), then the QAMF recommends that the case be assigned to a criminal investigation team. Once a case is assigned to an integrated criminal investigation team (or, where appropriate to a single organisation), the other parties do not pursue their own investigations.

The HK SFC has:

- entered into a Memorandum of Understanding (MoU) with the Hong Kong Police to formalise and strengthen cooperation in combating financial crime;
- signed a MoU with the Independent Commission Against Corruption, which lays out a framework for the mutual provision of investigative assistance, capacity building and case referrals as well as the exchange of information between the two organisations; and
- closely collaborated with the Hong Kong Monetary Authority to investigate authorised institutions' misconduct under the Securities and Futures Ordinance and with the Department of Justice on securities fraud, insider dealing, market manipulation and other offences.

ASIC has effective domestic relationships in place with relevant agencies to assist with deterrence of unlawful conduct. Memoranda of Understanding to facilitate cooperation are in place with agencies including (but not limited to) the Australian Federal Police, Australian Prudential Regulation Authority, Australian Competition and Consumer Commission, and Commonwealth Director of Public Prosecutions.

In Spain, nineteen private and public entities signed the Memorandum of Understanding for the Action Plan against Financial Fraud, as part of the fight against fraudulent offers of financial products and services, the increasing prevalence of which has been detected by the Comisión Nacional del Mercado de Valores (CNMV). The signatories will share technical and human resources and will create direct communication channels to speed up the exchange of information. The Action Plan mandates self-regulation to limit advertising by unauthorised entities; creates tools to inform bank customers of fraud risks; establishes information campaigns to warn the public about new fraud trends and promotes financial education. The CNMV has made its interactive database of pirate entities and financial boiler rooms available to the signatories.

## Regulatory affiliations

66. The credibility of enforcement may depend on external parties such as the police, prosecutorial authorities, and the courts. An impartial, effective, and efficient judicial system is critical to a legal and regulatory framework that deters misconduct.

## EXAMPLES

Many regulators also have arrangements whereby they liaise with the police and prosecutors whether at a case level or at a policy or strategic level.

The QAMF, like some of its sister regulators in Canada, maintains a constant and constructive dialogue with policy, administrative and judicial decision makers. In order to promote efficiency and effectiveness within the judicial system, it participates in a liaison committee with other prosecutorial authorities in Québec and the judiciary. This forum allows the QAMF to explain the issues surrounding its cases (complexity, administration of evidence) to the judiciary and to explore solutions.

The US SEC and the US CFTC work in close coordination with the Securities and Commodities Fraud Task Force, a unit under the Criminal Division of the US Department of Justice. The Task Force seeks to uncover fraud by investigating and prosecuting crimes relating to the operation of the securities and commodities markets in the United States, including all varieties of securities fraud, such as insider trading, market manipulation, accounting and regulatory reporting frauds<sup>34</sup>.

BaFin regularly participates in on-site inspections by the public prosecutors in market manipulation and insider dealing cases and assists police and prosecutors in evaluating evidence and thereby contributes specialised knowledge.

As violations of market abuse rules may entail the application of administrative and criminal sanctions, the legislation sets out special rules ensuring coordination between CONSOB and the prosecutor in a view of ensuring that the enforcement actions are effective and efficient. A specific protocol has been entered into to this purpose. CONSOB is also a signatory to protocols on cooperation with the financial police (Guardia di Finanza) to facilitate its supervisory activity. According to the law, CONSOB may avail itself of the cooperation of the finance police in the

<sup>34</sup> *Securities and Commodities Fraud Task Force, The United States Attorney's Office, Southern District of New York, US Department of Justice, available at <http://www.justice.gov/usao/nys/criminal.html>*

exercise of his powers. In particular, CONSOB may require the finance police: (i) to assist in the collection of information and documents useful for the purposes of an investigation; (ii) to carry out hearings, inspections, seizures, and searches on its behalf.

The US CFTC works closely with other federal and state civil and law enforcement agencies and participates in numerous federal and state government working groups and task forces to facilitate the sharing of information and expertise, develop best practices and coordinate, as appropriate, with civil and criminal authorities in connection with parallel enforcement matters. For example, the US CFTC entered into an agreement with the North American Securities Administrators Association (NASAA) to establish a closer working relationship, through individual MoUs with NASAA members, including state financial regulators, to facilitate enforcement of the Commodity Exchange Act, which U.S. state securities regulators and state attorneys general are statutorily authorized to do alongside the US CFTC<sup>35</sup>.

---

<sup>35</sup> <https://www.cftc.gov/PressRoom/PressReleases/7730-18>

## Factor 4: Investigation and prosecution of misconduct: Bold and resolute enforcement

### In brief

67. Commitment by a regulator to the early investigation, prosecution of misconduct and the flexible use of enforcement programmes that consider and adopt a range of strategies, investigative tools, and prosecutorial remedies, help to foster a regulatory environment in which misconduct is deterred.
68. Misconduct may be deterred when regulators:
- a.) are committed to the investigation and prosecution of contraventions;
  - b.) deliver enforcement outcomes in a timely manner;
  - c.) are invested with a variety of supervisory and enforcement powers, including compulsory powers to obtain assistance from registered and non-registered entities, and powers, either by executive action of the regulator or by application to a court, to sanction misconduct, by way of fines, disgorgement, restitution, prohibition, disqualification, or in the most serious of cases, imprisonment; and
  - d.) have the authority and discretion to access a variety of enforcement avenues including civil and criminal (including quasi-criminal) tribunals and courts settlement mechanisms and voluntary but enforceable agreements, where appropriate.

### EXAMPLES

The BCSC can sanction those who refuse to give information required for an investigation, or who destroy, conceal, or withhold evidence. The BCSC considers early settlement to be a factor that mitigates sanctions.

### In detail

#### Regulatory resolve

69. Credible enforcement requires a strong commitment to investigate and sanction misconduct, and this includes having both robust powers and a dedication to utilising them. Regulatory resolve may be demonstrated by regulators and regulatory decision-makers who are adequately resourced, who are empowered with the authority, flexibility and discretion to initiate investigation, litigation and prosecutorial action; who have the willingness and ability to impose a range of pecuniary and non-pecuniary sanctions and remedies; and who possess the necessary skills, experience and determination to exercise these powers competently to fulfil regulatory mandates and objectives. Enforcement programmes further demonstrate credibility when they are independent and have legal protections for acts undertaken in good faith.
70. Enforcement has greater relevance and impact if enforcement interventions and outcomes are delivered in a timely manner. Enforcement functions that have efficient decision-making practices and processes enhance deterrence by increasing the prospects of stopping misconduct early or at least delivering a deterrent message before the misconduct is considered historic. Regulators may want to review investigative practices and decision-making processes where impediments to timely and effective enforcement interventions are identified.
71. If legal and regulatory obstacles to timeliness exist, jurisdictions should consider whether legislative or regulatory reforms are appropriate to ensure that investigations and enforcement related proceedings whether at first instance or on appeal, progress expeditiously.

72. In order to foster timeliness, regulators should be armed with appropriate resources and tools to detect misconduct when it occurs, and to impede its proliferation through early intervention strategies. Regulators should be empowered to intervene, prosecute and sanction the misconduct in a timely manner.
73. Enforcement outcomes have greater relevance and impact on wrongdoers and victims if they are delivered as soon as possible after the misconduct has occurred. Likewise, it is unfair for an accused to be deprived of the right to be heard expeditiously. Regulators should therefore act to expedite enforcement actions so that justice is administered in a timely manner.
74. Encouraging co-operation with investigations may enhance timeliness and leverage a regulator's effectiveness by enabling the efficient use of regulatory resources. Money Laundering Reporting Officers and compliance and similar staff at authorised firms are uniquely positioned to assist regulators in early detection of contraventions and may encourage credible deterrence generally. Strategies that incentivise co-operation with regulators and other enforcement authorities (both domestically and internationally) by promoting compliance and reporting misconduct can bolster the regulator's efforts towards deterrence by allowing scarce resources to be redirected to other strategies and tools. This would include whistleblower regimes that create mechanisms for reporting misconduct within an authorised firm or to the regulator and provide whistleblowers with legal protection from victimisation.
75. One method of reducing the time and challenges in bringing criminal proceedings before the courts is for the regulator to be granted statutory powers to prosecute offences in appropriate circumstances, for example market abuse and financial services cases involving fraud or dishonesty. Such an approach also reduces the lead time between the conclusion of the investigation and the bringing of charges. Another approach to ensuring timely and effective criminal prosecutions is to promote close cooperation between regulators and criminal authorities. If the evidence or seriousness of the misconduct is not conducive to criminal prosecution, then administrative sanctions may be more appropriate.

## EXAMPLES

Many jurisdictions have specialised administrative decisions committees, or tribunals with decision makers with relevant professional experience or specifically trained in securities laws. The administrative process often can be quicker and more efficient than litigating or prosecuting in court.

In many jurisdictions securities regulators work closely with law enforcement authorities and prosecutors to bring cases before courts of criminal jurisdiction.

The UK FCA was granted statutory prosecutorial powers under the Financial Services and Markets Act 2000 and is the main prosecuting authority for insider dealing and unauthorised financial services in the UK, working closely with the police and prosecuting authorities in criminal investigations. The FCA is also able to prosecute prescribed money laundering offences.

To enhance its effectiveness, the OSC Enforcement Branch set up a dedicated criminal investigation/prosecution unit with former police officers, former crown prosecutors, and others so it can: (i) conduct searches under search warrants; (ii) initiate quasi-criminal proceedings; (iii) co-operate with the police in investigations; and (iv) with the assistance of crown prosecutors, initiate proceedings under the Criminal Code of Canada.

ASIC also has an agreement with Australia's Federal prosecution agency (the Commonwealth Director of Public Prosecutions) allowing ASIC to prosecute certain minor regulatory offences

itself, particularly 'high volume' prosecutions in relation to strict liability summary offences.

In February 2021, ASIC announced that it would consider and grant (subject to certain criteria) immunity to individuals who self-report misconduct from civil penalty or criminal proceedings of serious corporation's law contraventions if that individual was the first applicant for immunity and intended to cooperate with ASIC in relation to its investigation, and any subsequent court proceedings regarding the contravention. ASIC's immunity policy is based on a recognition that it may be in the public interest to provide an incentive to individuals who have combined with others to break the law, to reveal misconduct that may otherwise have remained undiscovered. The immunity policy does not cover immunity from administrative or compensation proceedings.

Belgium Financial Services and Markets Authority (FSMA)'s production and intervention powers allow regulators to react to new risky or complex products. In Belgium, the FSMA banned the marketing to retail clients of financial products whose return depends directly or indirectly on virtual money (namely Bitcoin derivatives).

To maximise resources and promote expediency in conducting investigations and addressing misconduct, the US CFTC Division of Enforcement has implemented a number of policies designed to promote prompt action such as providing incentives in the form of reduced sanctions for co-operating with an investigation through actions such as self-reporting contraventions, providing material assistance with the investigation, mitigation and remediation of any harm and agreeing to a timely settlement<sup>36</sup>. Additionally, the Commodity Exchange Act authorises the US CFTC to seek injunctive relief in federal court, which may include immediate interim relief such as restraining orders and asset freezes.

The HK SFC grouped together multiple cases which a firm might be involved in and resolving these in a single resolution. This is a deliberate effort to target systemic issues. Where it identifies multiple failings within a company or corporate group, it may consider these together and assess whether they are attributable to systemic weaknesses. It will more likely adopt this approach where the failings identified have not caused losses to clients or the investing public. The HK SFC is committed to using its resources efficiently and strategically to take enforcement actions that send clear and strong deterrent messages to the public and promote a good compliance culture amongst major market players. Taking a holistic enforcement approach to tackle systemic issues can be an effective way to achieve this.

Guernsey Financial Services Commission (GFSC) has comprehensive powers across all regulated sectors through one Enforcement Powers Law, which includes the appointment of inspectors, where we see recidivists, systemic breaches of the regulatory laws, rules, codes, and guidance. The licensee will pay the price of the inspector appointment who will investigate and report their findings to the GFSC.

### **Comprehensive powers**

76. In general, the greater the diversity and flexibility of supervisory and enforcement powers and remedial tools, the more effective regulators can be. This includes powers that provide regulators and regulatory and judicial decision makers with the authority, flexibility, and discretion to take timely action and to impose a range of pecuniary and non-pecuniary sanctions and remedies.
77. Powers that may enhance regulatory responsiveness include executive powers to:

---

<sup>36</sup> <https://www.cftc.gov/sites/default>

- a.) Ban, suspend (prohibit), or disqualify individuals;
  - b.) prevent the issue of documents for the purpose of capital raising;
  - c.) impose prohibitions and restrictions on businesses, e.g., from entering into certain types of transactions, advertising, promotion or carrying on business in a specified manner;
  - d.) issue directions for prudential purposes, e.g., apply a specific provisioning or treatment for specified assets;
  - e.) provide a report, prepared by an independent or skilled person, e.g., on the adequacy and performance of systems and controls; or
  - f.) promptly stopping online illegal activities, including the power to shut down or block access to illegal websites, either directly or by seeking a legal order to do so.
- 78.** Regulatory responsiveness can also be enhanced when regulators have access to administrative and judicial decision makers who, during the course of investigations, are empowered to make urgent and interim orders, inter alia, to:
- a.) prevent the destruction of evidence;
  - b.) freeze assets;
  - c.) require persons and entities to cease and desist or be enjoined from certain behaviour;
  - d.) require a person to do an act or thing such as provide a full account; or
  - e.) prohibit a person from carrying on business in a certain way.
- 79.** There are additional powers that may enhance a regulator's ability to facilitate credible deterrence, both domestically and through international co-operation, including:
- a.) compulsory powers to obtain information from non-registered persons/entities, such as books and records and testimony;
  - b.) more expansive compulsory powers applicable to registered persons/entities, including compulsory inspections and seizure of information and documents, the ability to direct authorised firms and individual registrants to provide specific assistance to the regulator, such as requiring the authorised firm or individual to undertake an independent review or analysis, to prepare and provide reports of independent reviews, or to otherwise act or refrain from acting in a particular manner;
  - c.) Auditing Information including, but not limited to, audit work papers, communications and other information relating to the audit or review of financial statements;
  - d.) Subscriber records held or maintained by telephone service providers who are located within the jurisdiction of the Requested Authority;
  - e.) Subscriber records held or maintained by internet service providers, and other electronic communication providers, who are located within the jurisdiction of the Requested Authority;
  - f.) Recordings of telephone conversations or other electronic communications held or maintained by authorised firms;
  - g.) the power to enjoin and sanction non-compliance with any requirements imposed by the

regulator, to order remedial action, or to suspend or revoke a licence or authorisation;

- h.) preventative powers to seek remedies such as, officer and director bans, and bans from performing financial services or professional functions within the jurisdiction of the regulator; and
- i.) sanctioning powers, either by administrative action of the regulator or by application to a court, such as orders for remedial actions, sanctions or censures, disgorgement, restitution, asset freezes and appointment of liquidators or administrators.

## EXAMPLES

Many regulators have the authority to seek telecommunications records and data. For example, the UK FCA is one of a number of agencies in the UK which is authorised under the Investigatory Powers Act 2016 to obtain communications data such as telephone and internet records from Communication and Internet Service Providers and to conduct directed surveillance, both physically and online, under the powers conferred by the Regulation of Investigatory Powers Act 2000. Under both pieces of legislation, the agency can only use these powers where it can show that their use is justified, necessary and proportionate and is in the context of the prevention or detection of crime.

In some jurisdictions, where the regulator discovers a person has contravened relevant rules, it has the power to suspend that person's permission to conduct investment business for such period as it considers appropriate. The UK FCA takes the view that misconduct includes non-financial misconduct. In a number of cases, the UK FCA has prohibited individuals from working in the financial services industry where they have been convicted of serious non-financial indictable offences while working in the industry.

Many regulators have the power to appoint administrators, i.e., receivers, managers and liquidators to institutions that find themselves in financial distress. Some jurisdictions are implementing resolution frameworks, such as living wills to accommodate financial failures in systemically important financial institutions.

Subsection 127(1) of Ontario's Securities Act gives the Capital Markets Tribunal the power to make various orders if, in the opinion of the Capital Markets Tribunal, it is in the public interest to do so. The Supreme Court of Canada has confirmed that the OSC has a wide discretion to intervene in activities related to the Ontario capital markets when it is in the public interest to do so. It is left to the OSC to determine whether and how to intervene in a particular case. While the power is broad, it is not unlimited. The Capital Markets Tribunal's jurisdiction under subsection 127(1) is neither remedial nor punitive. Rather, its authority is prospective in operation and preventative in nature.

The DFSA has the authority to enter the business premises (without warrant) of any person if that person may be able to give information or produce a document relevant to an investigation.

The US CFTC requires, subject to certain limitations, futures commission merchants, retail foreign exchange dealers, introducing brokers, and members of designated contract markets or swap execution facilities to maintain all oral and written communications provided or received concerning quotes, solicitations, bids, offers, instructions, trading and prices that lead to the execution of a transaction in a security, commodity interest and related cash or forward transactions, including those communicated by telephone, voicemail, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media. Such books and records

must be retained and produced under the registrants' regular record-keeping obligations<sup>37</sup>, which include a requirement to make them available for inspection, at the premises where they are kept, by any representative of the US CFTC.

In March 2019, the Australian Government introduced an enhanced corporate penalty regime which increased maximum prison terms for most serious offences in addition to higher civil penalties for individuals and companies. Under the new penalty provisions:

- maximum prison penalties for the most serious offences were increased to 15 years including breaches of director's duties, false or misleading disclosure and dishonest conduct;
- maximum civil penalties for individuals and companies were significantly increased;
- civil penalties now apply to a greater range of misconduct – including a licensee's failure to act efficiently, honestly, and fairly, failure to notify about reportable situations and defective disclosure; and
- the maximum civil penalty for individuals is now the greater of 5,000 penalty units (currently \$1.11 million) or three times the benefit obtained, and detriment avoided.

CONSOB can, pursuant to the national legislative framework, with regard to anyone who offers or carries out investment services via web without being qualified, order that the unauthorized investment services provider cease the infringement. Furthermore, CONSOB can suspend and/or prohibit the public offering of financial instruments and other financial products (and the related advertising) carried out without a prospectus. Moreover, CONSOB can directly order the providers of Internet connectivity, operators of other telecommunication networks and providers of telecommunication services to ban the access to the website (including foreign website) from Italy. The power can be exercised in cases of unauthorised provision of investment services/activities as well as in cases of public offers of financial instruments/products without prospectus.

The HK SFC uses the full spectrum of sanctions and remedies available to it under the Securities and Futures Ordinance, including through criminal, administrative, compensatory, and disciplinary actions. It has broad powers to hold directors and individuals responsible for misconduct committed by the companies they manage. The HK SFC can discipline licensed intermediaries through reprimands, fines and suspensions or revocations of licences, and apply to the court for injunctive and remedial orders against wrongdoers in favour of victims. In dealing with market misconduct, such as insider dealing and market manipulation, the HK SFC can institute criminal prosecutions or bring cases directly to the Market Misconduct Tribunal.

The GFSC uses the full suite of sanctions available to it to bring a licensee back into regulatory compliance, or to seek to prohibit individuals, or issue discretionary financial penalties. It can also suspend, or revoke a licence, and further make application to the court to place entities into administration or liquidation as appropriate.

Swiss Financial Market Supervisory Authority (FINMA) may appoint, by way of an order, an independent and suitably qualified person, (an investigating agent) to conduct investigations of regulated persons and implement regulatory measures that it has ordered. The regulated person or entity must allow the investigating agent access to its premises and provide him or her with all the information and documents that the investigating agent requires to fulfil his or her duties. The costs of the investigating agent are borne by the person or entity under investigation. The person or entity must, if so instructed by FINMA, make an advance payment to cover costs<sup>38</sup>. The appointment of investigating agents has proved an efficient and flexible measure to investigate complex circumstances, where FINMA has an initial suspicion that rules governing financial market regulation have been contravened. FINMA uses the instrument of the investigating agent most often to investigate and liquidate entities that provide financial services without having the

<sup>37</sup> CFTC Regulations 1.31 and 1.35, 17 C.F.R. 1.31 and 1.35 available at <http://www.ecfr.gov/cgi-bin/text>

<sup>38</sup> Art. 36 of the Swiss Financial Market Supervision Act (FINMASA). For an unofficial English translation of the FINMASA, see <http://www.admin.ch/ch/e/rs/9/956.1.en.pdf>

necessary licence or competence.

The US CFTC has numerous tools available to investigate potential misconduct and impose sanctions on those who have contravened the Commodity Exchange Act or Commission Regulations. The US CFTC is empowered to grant staff the authority to issue administrative subpoenas for documents and testimony from entities and individuals regardless of registration status with the US CFTC<sup>39</sup>. The latter is also empowered to pursue an enforcement action via federal court or administratively and may seek a variety of sanctions, including monetary penalties as well as injunctive relief such as asset freezes, an accounting of assets, the imposition of trading bans or a monitorship<sup>40</sup>.

From October 2021, ASIC has new regulatory powers under the Design and Distribution Obligations (DDO) and Product Intervention Powers (PIP), which allow for targeted prevention of harm for consumers of financial products. The DDO requires issuers and distributors of financial products to have adequate product governance frameworks to ensure their financial products are targeted at the right consumers. The PIP allows ASIC to request information and issue stop orders on financial products where it identifies a risk of significant consumer harm. Contraventions of the DDO can result in enforcement action, including seeking civil and criminal penalties through the Courts.

ASIC successfully obtained a court order compelling a company to produce certain documents required under a compulsory notice after the entity resisted production, arguing, *inter alia*, that ASIC was not entitled to seek such a broad range of documents. The court held the notice was validly issued and while the notice sought many documents, this did not mean the notice was too broad. In determining the company had no reasonable excuse for its non-compliance, the court held that 'inconvenience and expense would not ordinarily provide a reasonable excuse for non-compliance'.

ASIC successfully challenged a claim of client legal privilege made by an entity over an internal report, which the entity claimed was prepared at the direction of an in-house lawyer for the purposes of the lawyer giving legal advice. The entity had previously produced copies of the report to ASIC without objection. The court found that the entity did not provide sufficient evidence to establish that the report was privileged. And further, the court held that, even if the report had been privileged, the entity had waived its privilege by previously producing copies to ASIC without objection.

SEBI has broad investigative powers to unearth contraventions of securities laws by any intermediaries, market participants and persons associated with securities markets, including obtaining call data records from Telecom Service and banking records and statements to establish fund trails.

Pending investigation, SEBI has been vested with wide powers under the statute to suspend the trading of any security in a recognised stock exchange, including restraining persons from accessing the securities market and prohibiting any person associated with securities market to buy, sell or deal in securities; suspending any office-bearer of any stock exchange or self-regulatory organisation from holding such position; impounding and retaining the proceeds or securities in respect of any transaction that is under investigation. After the conclusion of inquiry, SEBI can make any direction it deems appropriate.

Bar certain exceptions, the OSC has the ability, on its own behalf, and on behalf of foreign securities regulators, to summon and enforce the attendance of any person and to compel him or

---

<sup>39</sup> 7 U.S.C. § 9(5)

<sup>40</sup> 7 U.S.C. § 9, 13a-1

her to testify on oath or otherwise, and to summon and compel any person or company to produce documents and other things. The refusal of a person to attend or to answer questions or of a person or company to produce such documents or other things as are in his, her or its custody or possession makes the person or company liable to potential contempt proceedings.

### **Avenues for enforcement**

80. Deterrence can be enhanced when a regulator has the authority and discretion to access diverse avenues for enforcement, including administrative, civil (including civil cases that permit the imposition of a penalty) and criminal (including quasi-criminal) tribunals and courts and early resolution and settlement mechanisms where appropriate. Regulators should consider prioritising those avenues that deliver the most efficient and effective sanctions and remedies.
81. Regulators and administrative and judicial decision makers should be empowered with a suite of sanctioning powers and remedies that best address a wide range of misconduct and the national and global impact of misconduct. Credible deterrence can be achieved if regulators and other decision makers have available to them a range of available sanctions.

### **EXAMPLES**

Many regulators have the authority to seek relief through the civil courts both on their own action and on behalf of investors or consumers, including for the recovery of loss and compensation.

Some regulators are empowered to commence civil proceedings and criminal prosecutions and to take action on behalf of investors and other third parties, in the place of private action by those parties, against financial markets participants. This enables regulators to address both conduct and compensation recovery issues for investors. Some jurisdictions require public interest grounds for action.

In a number of jurisdictions, regulators can bring a case before an administrative tribunal or a civil or criminal judicial authority. Often, when the misconduct warrants it or as necessary to obtain sufficient relief, the regulator will bring proceedings before more than one authority. The judicial authorities can impose a range of orders that may include pecuniary and non-pecuniary sanctions, injunctions and civil monetary penalties for the disgorgement of illegal profits or for losses avoided. Administrative sanctions may include cease-and-desist orders, suspension of broker-dealer and investment advisor registrations, bans, such as industry, equity security, officer and director bans, and bans from performing financial services functions within the jurisdiction of the regulator, as well as civil monetary penalties, disgorgement and undertakings.

In Canada, quasi-criminal proceedings, with concomitant heavier sanctions and potential prison terms, can be initiated with respect to certain types of securities sanctions.

The UK FCA has a range of avenues available to take action. In addition to its regulatory powers, it is able to commence civil or criminal proceedings through the courts. The FCA recently instigated criminal proceedings against National Westminster Bank for offences under the Money Laundering Regulations. This was its first criminal prosecution under those regulations.

ASIC has employed a combination of supervisory and enforcement powers to address the significant harms caused to retail clients by highly leveraged and complex products such as contracts for difference. ASIC has taken civil action against entities that offer these products who engage in high-pressured sales tactics and make false or misleading representations to consumers. In addition, ASIC has taken administrative action to reduce the risk of future harm, including by suspending the authorisation of certain financial firms and using ASIC's product

intervention powers to impose conditions on the issue and distribution of such products to retail consumers.

SEBI can employ a wide range of enforcement actions including cease and desist order, suspension or cancellation of registration, disgorgement, debarment, directions, freezing of assets and imposition of monetary penalty. SEBI can prosecute entities for contravening securities laws. Further, special courts have been established to expedite trials for such offences.

82. Some IOSCO member jurisdictions have found that special purpose administrative structures and tribunals, administered by regulators, are efficient and effective mechanisms and avenues for sanctioning securities contraventions.

### EXAMPLES

The QAMF has established an independent and specialised administrative tribunal for securities and derivatives (the Tribunal des Marchés Financiers or TMF) to deal with nearly all administrative requests made by the QAMF.

The DFSA has established an administrative decision-making committee, formed from senior staff members of the DFSA or suitable external professionals, that makes decisions about whether contraventions have occurred and if so, the sanction that should be imposed, including financial penalties and restrictions on performing financial services functions in or from the Dubai International Financial Centre.

The US CFTC has commenced enforcement actions by filing complaints through its administrative process in which all proceedings are conducted by a Presiding Officer with specialised knowledge<sup>41</sup>.

83. Aggrieved parties in some jurisdictions may also bring their own actions before tribunals and courts to seek redress.

### EXAMPLES

Many jurisdictions permit aggrieved parties (including by private right or class action), or regulators to join with aggrieved parties to pursue relief (including compensation), through the civil courts or administrative programmes for breaches of financial services laws and regulations.

Case law in the United States has established a private right of action for fraud in connection with the purchase or sale of securities and the US Commodity Exchange Act, administered by the US CFTC, explicitly provides for a private cause of action. The US CFTC also operates a reparations programme which provides a forum to resolve disputes between customers and registered trading professionals, which will be decided by a US CFTC judgment officer<sup>42</sup>.

### Incentives, co-operation, and settlement

84. The ability to settle with the subjects of investigations of enforcement proceedings, including settlement, deferred and non-prosecution agreements with a party can result in timely and cost-

<sup>41</sup> <https://www.cftc.gov/PressRoom/PressReleases/8229-20>; 17 C.F.R. § 10.1 et seq.

<sup>42</sup> <https://www.cftc.gov/LearnAndProtect/ReparationsProgram/index.htm>

effective resolutions that avoid the costs and complexities of administrative and court proceedings. Such settlements may also include restitution or remediation, in addition to punitive sanctions. In some cases, it may include a mechanism to obtain evidence from the party necessary to prosecute a more culpable party.

85. Settlement agreements can be more flexible in securing a variety of outcomes and remedies, including the imposition of remedial actions to strengthen systems and controls and risk mitigation strategies or other undertakings not always available in civil or criminal proceedings. Settlement agreements may also include admissions of misconduct, which can lead to greater accountability for the wrongdoer and greater clarity to investors and the public.

## EXAMPLES

Many regulators have the power to enter into agreements with licensees/registrants in disciplinary proceedings<sup>43</sup> or to use other voluntary but enforceable undertakings or settlement mechanisms prior to the imposition of a final decision by a formal decision-making body, such as an administrative tribunal or a court. The UK FCA makes use of an instrument called a *Voluntary Requirement* and can require firms to examine their conduct and address harm. In many cases, the FCA will ask firms to voluntarily accept a variation of permission or the imposition of a requirement (VREQ). If firms refuse the FCA may impose the variation or requirement under the FCA's own initiative powers (OIREQ). ASIC<sup>44</sup> and the DFSA<sup>45</sup> make use of enforceable settlement agreements called Enforceable Undertakings. These instruments allow regulators to achieve creative enforcement outcomes that may include remedies outside the normal range of sanctions.

The US SEC's Division of Enforcement has developed a series of measures designed to encourage greater cooperation by individuals and companies in US SEC investigations and enforcement actions. The programme provides incentives to individuals and companies who come forward and provide valuable information to US SEC investigators. The US SEC uses an analytical framework to evaluate whether, how much, and in what manner, to credit the cooperation by individuals and companies in its investigations and enforcement actions<sup>46</sup>.

The US CFTC Division of Enforcement has issued public guidance regarding several aspects of its practices for the evaluation and consideration of cooperation and remediation in the context of settlement agreements, primarily highlighting the potential for a reduction in the otherwise applicable civil monetary penalty emphasising that the most significant reductions would apply to those who self-report and engage in full cooperation and remediation<sup>47</sup>. In certain circumstances, the Division may enter into a Cooperation Agreements, Non-Prosecution Agreements, or Deferred Prosecution Agreements<sup>48</sup>.

The US CFTC frequently resolves matters through administrative settlements providing greater efficiency and certainty of the result and conservation of resources for all parties. In an administrative order, the US CFTC is authorised to make findings of fact, impose a civil monetary penalty, and impose a cease-and-desist order and on-exchange trading bans, require, payment of restitution, as well as other terms or undertakings agreed to by the parties. Such undertakings may include remedial action, broader prohibitions on trading, registration and other commodity interest related activities, or the appointment of a monitor.

43 Section 201 of the Hong Kong Securities and Futures Ordinance, available at <http://www.hkllii.hk/eng/hk/legis/ord/571/s201.html>.

44 Sections 93 & 93AA, Australian Securities and Investments Commission Act, 1989 available at <http://www.comlaw.gov.au/Details/C2005C00461>

45 Article 89 - Enforceable Undertakings, Regulatory Law, DIFC Law No 1 of 2004 available at [http://dfsa.complinet.com/net\\_file\\_store/](http://dfsa.complinet.com/net_file_store/)

46 See <http://www.sec.gov/spotlight/enfcoopinitiative.shtml>

47 <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/>

48 <https://www.cftc.gov/LawRegulation/Enforcement/EnforcementManual.pdf>

Like many regulators, the UK FCA provides incentives to those who settle its investigations early by discounting penalties that would otherwise be imposed. The UK FCA approach to settling cases is set out in DEPP. A discount of 30% of the penalty which otherwise might have been payable, may be obtained where cases settle early. This discount is available where a case is fully resolved (settled) or where the only issue in dispute is the financial penalty. Under the partly contested cases regime it is also possible to obtain discounts ranging from 0-30% depending on how much of the case is agreed. The period for any suspension, restriction, condition, or disciplinary prohibition that was to be imposed may also be reduced.

The OSC has a relatively new Disruptions and Partnerships Team. Among other things, the team takes steps that are alternative to typical enforcement investigative and prosecutorial action to disrupt incipient and / or ongoing illegal and potentially illegal activity. Disruptive action can take place in a variety of ways, and includes:

- the posting of investor warnings to the Ontario Securities Commission's website as well as to IOSCO's website;
- the publication of investor alerts in conjunction with other Canadian securities regulators
- the issuance of warning letters;
- dialogue with facilitators (such as internet registrars / web hosting companies) to disrupt, for example, potentially illegal websites; and
- "door-knocks" whereby staff of the OSC work with local police to conduct in-person visits to individuals to identify (and disrupt), through warning letters, illegal or potentially illegal activity.

The HK SFC issued an updated Guidance Note on Cooperation with the SFC to highlight the benefits of cooperating in its investigations and enforcement proceedings. The guidance note also introduces new measures to encourage cooperation which helps the HK SFC investigate more serious legal or regulatory breaches and achieve timely and desirable enforcement outcomes. The new measures include a section on civil proceedings, which describes its current practice of resolving proceedings in the civil court or the Market Misconduct Tribunal with cooperative parties and highlights the benefits of cooperating with the HK SFC in civil proceedings. There is also an updated section on disciplinary matters: it has divided its disciplinary process into three stages and added caps on the sanction reduction a party may receive for cooperating and resolving proceedings at each stage (bar exceptional circumstances which may warrant a further reduction).

## Factor 5: Sanctions: Strong punishments - no profit from misconduct

### In brief

- 86.** Regulators should have a range of sanctions that are effective, proportionate, and dissuasive. The sanctions should be greater than the cost of the misconduct so that the threat of the penalty removes the incentive for choosing not to comply. Sanctions should reflect the seriousness of the misconduct and aim to deter it. Sanctions that account for wrongful profits, compensate and restore victims and have an appropriate penal element enhance deterrence. In addition, deterrence can be enhanced when individuals are held personally accountable for their actions.
- 87.** Misconduct can be deterred when regulators:
- a.) demonstrate a willingness to impose or seek the imposition of sanctions and remedies that are effective, proportionate, and dissuasive;
  - b.) have at their disposal sanctions that appropriately respond to a wide range of evolving types of misconduct;
  - c.) have access to an appropriate range of administrative and judicial avenues for the imposition of sanctions;
  - d.) advocate that their administrative and judicial decision makers be empowered with a suite of sanctioning powers and remedies that best address misconduct and the impact of that conduct;
  - e.) hold individuals and entities, including those that are gatekeepers (such as accountants and lawyers) accountable;
  - f.) seek practical and innovative sanctions and remedies that best serve the investors and public interest; and
  - g.) where appropriate, seek to recover the cost of their investigations, prosecutions, and litigation from wrongdoers.

### In detail

- 88.** As a starting point, sanctions should seek to send the deterrent message that those involved in misconduct should not profit from it. IOSCO contends that sanctions should be effective, proportionate and dissuasive<sup>49</sup>.
- 89.** Imposing sanctions that reflect the seriousness of the misconduct should deter further misconduct. For instance, fines should not simply be a cost of doing business and recidivists should know that they will find themselves subject to tougher sanctions should they reoffend. A robust sanctioning regime provides a deterrent to misconduct if the potential costs of committing the contravention are perceived to outweigh the potential benefits.
- 90.** Robust sanctions can act as a catalyst to encourage propriety and compliance with laws, regulations and standards of behaviour. The credibility of any deterrence programme relies on the resolve of those who are responsible for its administration. If regulators are not willing to impose or seek the imposition of sanctions that are effective, proportionate and dissuasive, or if the system of enforcement is ineffective or perceived to be weak, then no matter how sound the rules are, the credibility of the regulatory framework could be undermined.

---

<sup>49</sup> *Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation* available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD359.pdf>

## EXAMPLES

Many regulators have broad powers to seek restitution, disgorgement of ill-gotten gains, penalties, and other punitive sanctions for a wide range of misconduct. Some regulators have the ability to seek penalties that are tied to the number of times the misconduct has occurred or that are multiples of gains achieved or losses avoided for certain contraventions, such as insider trading and market manipulation. For example, the Autorité des Marchés Financiers (AMF), France may seek penalties that are 10 times the profits made, or loss avoided.

Many regulators have the ability to make prohibition orders (e.g., excluding products from the market), direction orders, banning orders and stop orders, on a permanent or interim basis.

The QAMF seeks prison terms for every case of fraud or misappropriation of funds.

In March 2014, ASIC issued its Report 387 Penalties for Corporate Wrongdoing which explored how the penalties available to ASIC for corporate wrongdoing compared with penalties available internationally. The report considered penalties in Australia, Canada (Ontario), Hong Kong, the United Kingdom and the United States. The purpose was to allow ASIC to calibrate its response to breaches of the law with sanctions of greater or lesser severity commensurate with the misconduct, with the stated aim to deter other contraventions, and promote greater compliance, resulting in a more resilient financial system.

CONSOB's cooperation in the cross-border recovery of sanctions contributes to enhancing credible deterrence. Accordingly, forms of collaboration among IOSCO members to facilitate cross-border recovery of monetary sanctions could also contribute to deliver credible deterrence.

## Setting of sanctions

91. Regulators should explore practical and innovative sanctions and remedies that best serve the public interest and the interests of investors and develop transparent criteria for the determination of sanctions and fines. Multi-fold sanctions may be necessary to deter certain behaviour.

## EXAMPLES

In insider trading cases, several regulators can obtain penalties that are multiples of the amounts of profit gained or loss avoided.

For example, in Italy, the law, in compliance with relevant EU discipline, provides that the amount of administrative pecuniary sanctions for insider trading shall be increased up to three times or, where larger, ten times the profit generated or the losses avoided due to the unlawful action when, having taken account of the criteria for determining sanctions and the size of the product or the profit from the unlawful action, they appear to be inadequate even if the maximum is applied.

SEBI initiated the establishment of a database, hosted by the Asia-Pacific Regional Committee (APRC) of IOSCO, to track and store sanctions data of regulators who volunteer it. This data is a useful source of information for regulators, and administrative and judicial decision makers, who seek guidance as to the appropriateness of sanctions and remedies imposed for a range of market abuse and financial services contraventions. The database is held on the IOSCO website and is available for APRC regulators to contribute to on a voluntary basis.

In India, SEBI Act, 1992 lays down the factors which are to be taken into account while setting the

quantum of monetary penalty, namely – (i) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default, (ii) the amount of loss caused to an investor or group of investors as a result of the default, and (iii) the repetitive nature of the default.

SEBI is empowered to levy monetary penalty up to three times the profits in cases such as insider trading, fraudulent and unfair trading practices and non-disclosure of acquisition of shares and takeovers

In October 2020, Australia's Federal Court ordered the then largest penalty ever in a single enforcement action, which concerned over-the-counter derivatives. The serious nature of the contraventions and the need to send a strong deterrent message to the limited number of licensees dealing in the financial product justified the high penalty.

The UK FCA's penalties policy for misconduct has been in place since 2010. This framework was intended to create transparency in the way penalties are set, improve the consistency of penalties levied and also increase the levels of those penalties to achieve credible deterrence. The regime consists of a five-step process under three principles focusing on (i) disgorgement of profits made or losses avoided, (ii) discipline taking into account the seriousness, nature and impact of the breach and any aggravating or mitigating factors, and (iii) deterrence to the subject and the market.

The penalty regime is referred to in the FCA's published Decision Notices. A Decision Notice will detail the alleged breaches, the reasons for the decision taken, the proposed sanction and the right to require a referral to the upper Tribunal, which is independent of the FCA.

The UK FCA has introduced the Senior Managers and Certification Regime (SM&CR) a new accountability framework focused on senior management. At first the SM&CR applied to the banking sector before it was recently extended to all UK FCA-authorized firms. The SM&CR aims to reduce harm to consumers and strengthen market integrity by making individuals more accountable for their conduct and competence. The Senior Manager's Regime makes senior managers more responsible and accountable for their actions, and makes sure firms and individuals clearly understand and can demonstrate where responsibility lies. Senior Managers are expected to actively discharge their responsibilities, by taking reasonable steps to ensure the firm is being run well. The Certification Regime places responsibility on firms for ensuring their employees are fit and proper. The Conduct Rules set a new standard of personal conduct, against which individuals can be held to account.

The Commodity Exchange Act (CEA) authorises civil monetary penalties for each contravention of the CEA and Regulations, and it sets the maximum penalty per contravention<sup>50</sup>. Generally, penalties may be determined on a per contravention basis or up to triple the monetary gain, whichever is greater. Other remedies and monetary relief available in the US CFTC's enforcement proceedings include restitution and disgorgement. Additionally, the Division of Enforcement has issued public advisories detailing the factors it will consider in formulating its recommendation for a civil monetary penalty in a particular matter, including how cooperation will be taken into account<sup>51</sup>.

## Restorative measures

92. Competent authorities should consider the deterrent value of restorative measures that aim to compensate victims for their losses or restore them to the position they occupied before the misconduct occurred.

---

<sup>50</sup> See 7 U.S.C. §§ 9(10), 13a, 13a-1(d)

<sup>51</sup> <https://www.cftc.gov/LawRegulation/Enforcement/EnforcementManual.pdf>

93. The restoration of victims and the acknowledgement of misconduct by wrongdoers are becoming more prevalent in the orders some regulators are seeking from judicial and administrative decision makers. Restorative measures focus on two principal themes: strengthening the accountability of the offender; and restoring the victim (as an individual person or entity, or society as a proxy victim) to their pre-misconduct position. The application of restorative measures to cases involving serious criminal offences may be effective in reducing recurrent misconduct. They can help promote the message that genuine accountability requires wrongdoers to do more than write a cheque.
94. Restorative orders may include orders for compensation, orders requiring the implementation of compliance or educative programmes, and reformative measures that involve the offender acknowledging their conduct and its impact. A measured and consistent strategy of seeking such orders in appropriate cases can assist to achieve credible deterrence.
95. In addition to other measures, recidivism may be reduced if there is rehabilitation assistance, including training, education, mentoring and other support from which offenders learn what good behaviour looks like and are able to discuss it with mentors or peers. Prison sentences alone will not prevent reoffending in all cases. Reoffending may be reduced if the offending party is required to adopt a range of remedial actions, some of which may be implemented after or concurrent with the punishment or sanction.

## EXAMPLES

Many securities regulators have both civil and administrative authority to seek restorative orders including, for example, an order that was obtained by the HK SFC that required an issuer to repurchase shares sold to thousands of investors where information within the prospectus was found to be misleading.

A restorative measure has been successfully applied in Australia, where the senior executives of an insurance company that had mis-sold insurance policies, travelled to meet the representatives of indigenous communities, members of which had been mis-sold insurance policies, in order to fully apprehend and understand the harm done.

Sanctions available to the US CFTC include restitution and disgorgement. Where restitution is ordered, a monitor is typically appointed to oversee the collection and distribution of any funds to be returned to investors. When appropriate, additional relief, such as an accounting of assets, may also be ordered. Unlike a private action alleging fraud in contravention of the Commodity Exchange Act, in an enforcement action brought by the US CFTC the law does not require the Commission to establish investor reliance on a false statement or material omission to establish a contravention. Accordingly, the US CFTC, through the Division of Enforcement, may have a more efficient path to recover losses on behalf of victims.

Belgian law introduces a rebuttable presumption for breaches of rules of conduct (such as mis-selling), so that investors no longer have to prove the causal relationship between the breach and the investment transaction. It is assumed that the investor would not have made the investment decision had the service provider not committed the breach. As a consequence, investors who have suffered losses because a service provider has committed a fault, will be more easily able to obtain compensation in court.

The BCSC, like its Canadian counterparts, uses Victim Impact Statements to assist sanction decision makers to make better decisions about proportionality. The BCSC collects information from victims which is collated and introduced as an exhibit at the Sanctions Hearing to enable decision makers to better fashion a punishment to fit the crime.

The US SEC has authority to return funds to injured investors by allowing civil penalties and the proceeds of disgorgement to be included in Fair Fund distributions to investors harmed by securities contraventions.

In India, SEBI has the power to issue directions for disgorgement of unlawful gains made or notional losses averted thereby restoring the investors or public at large to their position prior to the contravention. Further, SEBI issues directions to refund moneys wrongfully raised or deposits wrongfully collected from the public, either by way of fees/ subscriptions, etc. SEBI also has the power to recover any dues thus payable by entities (i.e., payable either as penalties, refunds, or disgorgement amounts), and can attach bank accounts, and movable and immovable properties for such recovery.

96. Mechanisms that seek to ensure payment of pecuniary sanctions, such as the powers to order accountings, appoint receivers, and freeze assets, can enhance deterrence.
97. Sanctioning decisions should have regard to the context, nature, gravity, impact and victims of the misconduct and to the public interest. For example, to the extent possible and appropriate:
  - a.) individuals and entities should be held accountable for, and not profit from, their unlawful acts or omissions;
  - b.) penalties should constitute fines above and beyond unlawful profits;
  - c.) investors should be protected, and restored by the perpetrator to the position they occupied before the misconduct;
  - d.) recidivists should be subject to more stringent sanctions;
  - e.) remedies should seek to strengthen the integrity and governance of regulated entities and public companies;
  - f.) the level of co-operation by wrongdoers should be considered in sanctioning decisions;
  - g.) the obstruction of investigations should be treated as an aggravating factor; and
  - h.) criminal sanctions should be available for egregious contraventions.

### **Individual accountability**

98. It is common practice for regulators to impose sanctions on institutions. However, the conduct of institutions is governed and carried out by individuals. Therefore, regulators should consider whether it is appropriate to also hold those individuals accountable. Holding individuals accountable can reinforce acceptable standards of behaviour in individuals and institutions and can be a critical factor in deterring misconduct. Regulators should therefore consider developing a culture of accountability in their public messaging, laws, enforcement strategies and prosecutions to punish egregious misconduct and reinforce compliant behaviour.

### **EXAMPLES**

The competing needs of investors, creditors and other interested parties are relevant to individual sanctions. In November 2020, ASIC successfully sought to recover a penalty from a director but not the company, as doing so would have decreased funds available to creditors. The outcome

sent an important message that ASIC will take action to hold gatekeepers to account.

Whilst many jurisdictions have conferred on their competent authorities the discretionary power to ban persons from management functions in licensed financial institutions, Belgian legislation goes a step further by introducing an additional automatic ban within the financial industry on persons in management positions who have had a criminal or civil sanction imposed on them. This means in practice that these persons are automatically banned from occupying effective management positions in banks or other financial institutions. The automatic ban following an administrative fine is for a period of 10 years.

The UK FCA has proposed changes to the way individuals working for certain authorised firms are assessed and held accountable for the roles they perform. In particular, the proposed amendments would allow the UK FCA to impose conditions, time limits and variations on the approval of the senior managers of certain authorised firms and are designed to promote a clear allocation of responsibilities to senior managers and enhance their individual accountability. Other changes have been proposed to introduce, in respect of certain senior individuals, a requirement for a minimum claw-back period for variable remuneration, and to enhance the ability of firms to recover variable remuneration even if it has been paid out or vested<sup>52</sup>.

In India, section 27 of the SEBI Act, 1992 stipulates that in the case of any contravention of the securities laws by a company, the persons in charge of the said company would be liable for the said contravention. In cases of illegal money mobilisation, SEBI has fixed the liability to refund on the company as well as the officers in default who were in charge of the company at the relevant period of money mobilisation.

SEBI (Intermediaries) Regulations, 2008 empowers SEBI to debar an officer of any registered intermediary from being employed or associated with any registered intermediary or other person associated with the securities market for such period as may be specified.

Section 304 of the Sarbanes-Oxley Act allows the US SEC to hold individuals accountable by making CEOs and CFOs of public companies repay their company for certain compensation received during years when the company underwent an accounting restatement resulting from material non-compliance with financial reporting requirements, even if the CEO or CFO has not participated in the misconduct.

The US CFTC routinely pursues enforcement actions involving charges against one or more individuals, including individuals at all levels within financial institutions, proprietary trading firms, and managed funds and may seek sanctions such as trading bans, officer and director bars, or other remedies designed to prevent such individuals from participating in the markets within the US CFTC's jurisdiction.

In Italy, the law sets out specific cases under which, in addition to the application of sanctions against a regulated entity/issuer, CONSOB may impose sanctions against a person who performs administrative, management or control functions or an employee at the relevant regulated entity/issuer for violations of duties of such persons or of the body to which such person belongs. For example, it is possible to impose sanctions against the said individuals at the relevant regulated entity/issuer when the conduct had a significant impact on the overall organization or risk profile of the company or has caused serious harm to the protection of investors or to the transparency, integrity and proper functioning of the market. Moreover, CONSOB may impose sanctions against the aforesaid individuals at the relevant regulated entity when the breach

---

<sup>52</sup> <http://www.fca.org.uk/news/cp14-13-strengthening-accountability-in-banking> and <http://www.fca.org.uk/news/pr-14-13-and-fca-consult-on-proposals-to-improve-responsibility-and-accountability-in-the-banking-sector>

concerns obligations regarding remuneration and incentives.

99. Furthermore, regulators should consider holding individuals, who have important roles in financial activities and/or those that act as gatekeepers (e.g., compliance officers, accountants, auditors, officers/directors of public companies, etc.), accountable. These gatekeepers underpin the integrity of institutions and the financial services industry and are the first line of defence in the detection and remediation of misconduct. Sanctions for these persons could include such measures as criminal and civil penalties, but also, as appropriate, delicensing/deregistration and bans from the regulated industry or profession or from providing services to the regulated industry or from being an officer or director of a public company. Another deterrent sanction for gatekeepers is the claw-back of professional fees for services that facilitate misconduct, and the claw-back of bonus and incentive awards that were derived from such conduct.

### Cost recovery

100. In some jurisdictions, securities regulators are publicly funded. Some governments have determined that the public should not have to pay for the failures and misdeeds of others. Where such public-funded enforcement action has resulted in a finding of misconduct, regulators in those jurisdictions may consider recovering the cost of their investigations, prosecutions, and litigation from wrongdoers. Other jurisdictions might also consider developing efficient and effective cost recovery laws, policies and procedures to recover their costs as a factor in deterring misconduct. Would-be wrongdoers may think twice about contravening the law if they know that they might be required to pay for the regulators' investigation, litigation and/or prosecution of the contravention.

### EXAMPLES

The Qatar Financial Centre Regulatory Authority (QFCRA) pays the costs and expenses of an investigation, except if the person under investigation is found to have contravened a relevant requirement. In that case, the QFCRA or, where appropriate, the appeals body or tribunal may order that person to cover all or part of the costs and expenses of the investigation<sup>53</sup>.

Pursuant to the NZ Securities Market Act, where the NZ FMA obtains a pecuniary penalty award for insider trading and market manipulation, it is entitled to first recover its investigation costs from the sum paid before the remaining penalty is paid to the Crown (central treasury).

Under the Australian Securities and Investments Commission Act 2001, ASIC may make an order to recover its investigation expenses and costs if, as a result of its investigation:

- a person is convicted of an offence, or
- judgment is awarded, or a declaration or other order is made against a person in a proceeding in a court.

In 2018, the DFSA fined a broker USD202,500 for amongst other things failing to comply with a DFSA requirement for the production of documents. The broker's Chief Information Officer had prevented the DFSA from copying data required and deleted relevant data. As a consequence, the DFSA required the broker to pay USD100,000 towards the DFSA's investigation costs, as the broker's conduct caused the DFSA to incur considerable and otherwise unnecessary investigative expenses.

53 Article 50 of the Financial Services Regulations, Version 2, effective 9 December 2010, available at [http://www.complinet.com/qfcra/display/display.html?rbid=1557&element\\_id=859](http://www.complinet.com/qfcra/display/display.html?rbid=1557&element_id=859)

## Factor 6: Public messaging: Promoting public understanding and transparency

### In brief

- 101.** Public messaging can deter misconduct when would-be wrongdoers know that regulators will publicise enforcement outcomes and sanctions imposed against individuals and entities. Regulators who communicate their objectives, mandates and enforcement outcomes, and seek and respond to feedback, engender public support for regulatory and enforcement programmes.
- 102.** Misconduct can be deterred when regulators:
- a.) clearly explain their objectives and how they fulfil their mandates so that the regulated community and the public understand how and why regulations apply to them, how they are enforced and the consequences of non-compliance;
  - b.) clearly set out the behavioural expectations for market and industry participants through the publication of enforcement outcomes supplemented by guidance and other communications where necessary;
  - c.) make it known that individuals and entities will be held accountable for their actions;
  - d.) enhance transparency and compliance by making public all final enforcement decisions, including the publication of the identities of persons and entities against whom sanctions are imposed;
  - e.) issue public policies about the publication of investigation and enforcement actions; and
  - f.) alert the public about misconduct and bad selling practices, and high-risk products and services.

### In detail

#### Alerting investors

- 103.** It is common practice for regulators to inform and warn the public about scams and other fraudulent activity. Some regulators use innovative and bold practices to educate, inform and alert the public to potential and ongoing fraud.
- 104.** The increase in the use of the internet, especially social networks, accelerated as a consequence of the COVID-19 pandemic and has changed investor behaviour. Consequently, online fraud has also increased significantly, forcing regulators to intensify their efforts to disseminate information to protect investors.
- 105.** The use of social networks represents a new tool for relaying immediate information to investors with a preventive and informative purpose, and as a result, advances the fight against fraud, as well as increase the effectiveness of our supervision.

#### EXAMPLES

The CNMV, like other securities supervisors, publicises investor alerts about possible fraud on the internet, as well as through social networks, because of the need for immediate dissemination. Recently, alerts have also been disseminated through Twitter. Alerts issued include attempts to defraud investors using simulated telephone numbers, domains, or the image of the CNMV, as well as attempts to defraud investors using false identities of supervised and authorised entities.

ASIC has created fictitious websites and lured investors by using techniques frequently used by

fraudsters and offered rewards to members of the public who were able to identify their scams.

The US SEC's Division of Examinations provides the public with information on issues that it identifies through its National Exam Program that could be used to deter contraventions of the US securities laws. The Division has a number of tools to accomplish this, including publishing risk alerts and conducting outreach. In addition, annually the Division publishes its examination priorities to provide insights into its risk-based approach, including the areas it believes present potential risks to investors and the integrity of the US capital markets.

Furthermore, the SEC Office of Investor Education and Advocacy (OIEA) provides investor education and alerts through its website, <https://www.investor.gov/>. The website provides red flags for fraud, as well as registration background checks for Investment Advisers and Broker Dealers. Many of the SEC Divisions have their own social media pages, including Twitter, Facebook, and YouTube, where Investor Risk Alerts are also posted.

The US CFTC's Office of Customer Education and Outreach provides the public with information and resources to help investors avoid fraud. Information available through the learning resources page of the agency's website includes several articles, advisories, brochures and videos about common fraudulent schemes and directs consumers to additional resources such as NFA BASIC (<https://www.nfa.futures.org/basicnet/>) where they can check the background of financial professionals<sup>54</sup>. Additionally, the US CFTC's Whistleblower Office periodically publishes alerts on trending topics, such as spoofing, digital assets/virtual currency, Bank Secrecy Act, insider trading, and foreign corrupt practices to raise awareness of areas of particular interest to the Division of Enforcement and inform members of the public about how they become eligible for awards by helping to stop violations of the CEA.<sup>55</sup> The US CFTC also publishes a Registration Deficient List, known as the RED List, which contains names of foreign entities that appear to be acting in a capacity that requires registration with the US CFTC, but are NOT registered and advises the public to be cautious of unregistered firms or individuals when participating in products or markets that historically have seen a large number of fraud complaints<sup>56</sup>.

The HK SFC launched various campaigns through multiple channels to alert the public about the use of online platforms to defraud investors. In May 2021, the HK SFC launched an online campaign which simulated the experience of being drawn into an investment scam. In addition, the HK SFC has warned the public about online scams in media interviews and on its official Facebook page. It has also worked closely with the Hong Kong Police's Anti-Deception Coordination Centre to produce short videos and hold community outreach events to raise public awareness. Practical guidance on how to identify the warning signs of investment scams is also made available to the public by the Investor Financial Education Council, a HK SFC subsidiary.

## Transparent enforcement and accountability

- 106.** Publicity of enforcement actions can be effective for deterrence when it clearly explains what went wrong, how the sanction was determined and why the conduct breached the regulator's rules and principles. Publicity in cross border enforcement cases can be particularly powerful when regulators coordinate the timing and content of their announcements.

---

<sup>54</sup> <https://www.cftc.gov/LearnAndProtect/Resources/index.htm>

<sup>55</sup> <https://www.whistleblower.gov/whistleblower-alerts>

<sup>56</sup> <https://www.cftc.gov/LearnAndProtect/Resources/Check/redlist.htm>

107. Regulatory guides may assist in understanding the rationale behind enforcement actions.

#### EXAMPLES

ASIC publishes regulatory guides to assist in:

- Explaining when and how ASIC will exercise specific powers under legislation;
- Detailing how ASIC interprets the law; and
- Providing practical guidance (for instance describing the process to apply for a particular financial services license).

These guides strengthen understanding of the law and how it's enforced within the regulated community, fostering greater compliance.

- <https://asic.gov.au/regulatory-resources/find-a-document/find-a-regulatory-document/?docType=Regulatory%20guide>
- [[Regulatory Guide RG 211 Clearing and settlement facilities: Australian and overseas operators](#)]

108. Public messaging can promote deterrence by demonstrating that there are tangible consequences for those engaging or contemplating engagement in misconduct.

109. Regulators should, within their legal competence, consider publishing all final enforcement decisions including the identities of persons and entities against whom sanctions are imposed.

#### EXAMPLES

ASIC has an internal media unit and ASIC representatives give radio, television and print interviews in relation to high profile ASIC matters where it is deemed appropriate given the circumstances. ASIC also has a monthly podcast covering various topics including recent enforcement outcomes and industry relevant financial services issues. This keeps the general public and regulated community informed of ASIC's regulatory and enforcement activities, its expected standards of behaviour and focus areas of misconduct.

110. Providing the legal and factual basis for enforcement cases can enhance public understanding of regulation and assist in managing expectations. Those seeking to understand and comply with regulatory obligations are better able to make judgments and govern their institutions, people, and resources if they better understand the rationale for and consequence of enforcement action.

111. Moreover, informing the public about disciplinary actions against financial service professionals can have a strong deterrent effect particularly when individuals and entities are held accountable. Public messaging cautions that individuals and entities will be held accountable and that there are consequences for engaging in unlawful activity. Regulated persons can be expected to think twice before committing securities contraventions if they know their names and infractions are disclosed on a public record.

#### EXAMPLES

The UK FCA will not normally make public the fact that it is or is not investigating a particular matter before that investigation has reached the disciplinary stage. However, the UK FCA is permitted by legislation to publish Decision Notices and Final Notices, which provide detailed descriptions of the misconduct, the breaches, and the penalty. Decision Notices are issued when the UK FCA has decided what action to take, and Final Notices are issued when the matter has

been concluded. The UK FCA can also publish statements about Warning Notices, which are issued at the end of an investigation and at the very start of the disciplinary process. Unlike Decision and Final Notices, Warning Notices are not published in their entirety and might not name the subject of the Notice, but they are an important aid to early transparency which has benefit for consumers and financial services and market users. Publishing Notices is an important way for the UK FCA to show the behaviour that it considers unacceptable and encourage compliant behaviour, thereby enhancing confidence in the regulatory system. This practice also demonstrates openness about the enforcement process, which is important for public interest.

Article 34 of the Financial Market Supervision Act (FINMASA) gives FINMA the power to publish all or part of its final rulings on serious contraventions of supervisory law, including personal details of those involved, once a ruling has become legally binding and it provides for this (i.e., naming and shaming). FINMA makes a gradation in the assessment of the publication period (subject to the severity of the contravention, 1-3y, 4-5y, max. 10y). A list of rulings published under Article 34 FINMASA can be found on FINMA's website.

Furthermore, FINMA maintains and publishes a warning list of companies and individuals who may be carrying out unauthorised services and are not supervised by FINMA. FINMA checks the companies and individuals on its warning list to see if they are providing unauthorised services. The findings, however, have so far been inconclusive because the companies and individuals concerned have not complied with the requirement to provide information, or the information they provided is false. Moreover, when FINMA investigations reveal an imminent and considerable threat to investors, the providers involved are also entered in the warning list. The fact that a company is on FINMA's warning list does not mean that its activities are unlawful per se. Their entry in the list does, however, highlight the lack of authorisation. The companies and individuals in question will be removed from the list once FINMA has completed its investigations and taken any appropriate measures.

FINMA further publishes anonymised summaries of its enforcement actions and selected court decisions in a database.

It thereby increases the transparency of its activity in this area and shows the market what practices are unacceptable.

ASIC publicly reports on its enforcement activities every six months, including the number of investigations it has commenced and the number of prosecutions, civil penalties and administrative banning outcomes it has achieved. These enforcement updates send a clear message to the public that individuals and entities who have breached the law will be held accountable for their actions.

### **Timely publication**

**112.** The timeliness of the publication of information about enforcement actions, as well as possible investment scams, can deter those contemplating misconduct before it manifests into serious harm to investors. For example, regulators who alert the public about illegal schemes, unlawful fundraising activities, illegal selling practices, high risk products or misconduct, in a timely manner, are likely to deter misconduct and prevent consumers from being harmed.

### **EXAMPLES**

The Polish Financial Supervision Authority (KNF) proactively educates and informs the public about actions and risks relating to the operation of the financial market and entities operating on the market by publishing warnings and announcements, and broadcasting them on radio and television, in order to protect the justified interests of financial market participants. Furthermore,

the KNF may communicate to the public information about filings with the public prosecutor on suspicion of a breach of financial services legislation. This information is supplemented with an update on the final and binding refusal to initiate the preparatory proceedings or on the final and binding discontinuance of the preparatory proceedings and, in the event of the filing of an indictment, with an update on the final and binding court ruling.

The US CFTC promptly publishes on its website documents related to enforcement actions such as complaints, significant decisions, and final orders accompanied by a press release highlighting important details about the significance of a particular action or initiative taken by the Division. Relevant statistics and significant programmatic developments are compiled and published by the Division in an annual report.

SEBI promptly uploads its orders to its website following the passage of interim orders or conclusion of quasi-judicial proceedings. The order may include the following details: regulations and provisions contravened; consideration of reply filed by the entity; reasons for holding the entity liable; and the penalty imposed / debarment order / any other suitable direction issued to the entity.

## **Factor 7: Regulatory governance: Good governance delivering better enforcement**

### **In brief**

**113.** To keep pace with financial innovation and illicit practices, regulators should consider:

- a.) regularly reviewing regulatory and enforcement strategies, priorities, and tools; and
- b.) how they can identify innovative regulatory approaches to deal with such practices.

**114.** Misconduct can be deterred when regulators:

- a.) act to ensure regulation is well designed including regular reviews;
- b.) have the competence, resources, technology and resolve to investigate misconduct;
- c.) are independent and free from inappropriate political or industry influence;
- d.) have ready access to information, data, and performance metrics, including information about the effectiveness of their enforcement programmes, so that enforcement decisions can be made on an informed basis;
- e.) regularly review and assess the effectiveness of their governance and organisational arrangements and make reforms where necessary;
- f.) have appropriate levels of funding and access to skilled and experienced staff, intellectual capital, and innovative technology and practices;
- g.) look outside the field of enforcement to see what other innovative practices can be used to enhance deterrence;
- h.) have the appropriate regulatory tools to fulfil their mandates;
- i.) understand the drivers of good and bad behaviour and design regulatory programmes to respectively incentivise and sanction these types of behaviour; and
- j.) publicly report their performance to enhance public understanding of their objectives and effectiveness.

### **In detail**

**115.** Innovation in the finance industry has led to the development of new financial products and new ways of doing business. Those engaged in illicit practices have created innovative ways to engage in misconduct. They can more easily engage in cross border activities, conceal their identities, find refuge in poorly regulated jurisdictions, use advanced technologies and exploit weaknesses and gaps in laws and regulations. They use innovative products, sophisticated techniques and new technology to take advantage of unsophisticated investors. Regulators also need to innovate to keep pace.

### **Governance**

**116.** Governments, the regulated community, and investors expect regulators to deliver on their mandates and act in the public interest. Regulators can best fulfil their mandates if they are independent and free from inappropriate political or industry influence.

**117.** The characteristics of effective regulators include:

- a.) strong internal governance and decision-making capabilities;

- b.) structures that provide robust oversight, promote independence and objectivity; and
- c.) cultures that foster specialisation and innovation and facilitate information sharing and collaboration.

118. Regulatory design is often a function of the unique legal, economic, political, and social environment in which regulation functions. Whatever the regulatory model (i.e., twin peaks, integrated, industry-based or functional), enforcement programmes should be able to adapt their structures to respond to current and emerging risks. There is no one-model-fits-all solution. However, many regulators are adopting structures that favour specialisation.

119. Regulators seeking to maximise credible deterrence should consider regularly reviewing the effectiveness of their governance and organisational arrangements, particularly in their enforcement programmes.

## EXAMPLES

The UK FCA's Strategy and Competition Division acts as the UK FCA's radar in terms of spotting problems in financial markets early and designing strategies to solve them. It plays a vital role in enabling the UK FCA to act quickly and decisively when market issues appear on the horizon, and in delivering the UK FCA's mandate to promote effective competition. The Strategy and Competition Division shares intelligence and analysis with other areas of the UK FCA to make smart policy and strategy proposals. The UK FCA's Enforcement and Market Oversight Division also has a substantial strategy team which is responsible for ensuring that the Division's strategy, policies, and engagement are innovative and relevant. This team's responsibilities include: (i) the development and analysis of performance metrics; (ii) obtaining feedback from external stakeholders about the effectiveness of enforcement outcomes; (iii) liaising with international counterparts in the development of policies and strategies around international cooperation and, in terms of specific cross border cases, feeding into the legislative process at both the national level as well as the European level; and (iv) generally ensuring that the Division has the right powers, processes, policies and resources.

The UK FCA has recently launched an initiative known as *Project Innovate* to support UK businesses that are developing products that could improve services for consumers. This initiative provides for UK FCA assistance in preparing applications for authorisation and help in understanding the regulatory framework and is intended to identify areas where the regulatory framework could be adapted to allow for further innovation in the interests of consumers<sup>57</sup>.

The US CFTC has completed a reorganization to enhance operational effectiveness, resulting in the creation of new divisions, including the Division of Data and the Office of Technology Innovation. Additionally, the US CFTC's market surveillance program was merged into the Division of Enforcement to facilitate the identification of trading activity that warrants further enforcement inquiry. The Division of Enforcement also frequently creates Task Forces in novel or complex areas such as spoofing, insider trading, and digital assets to harness expertise and experience and promote collaboration and consistency across investigations and enforcement actions.

SEBI has a dedicated department called the "Corporation Finance Investigation Department" (CFID). The primary objective of this department is to holistically investigate securities laws contraventions involving different components of the financial reporting processes, including integrity and accuracy in financial statements and other issuer disclosures. The CFID is a specialised investigation department for the early detection and examination of fraud in financial statements, and of financial irregularities by the listed entities. The CFID also has a panel of

---

57 <http://www.fca.org.uk/firms/firm-types/project-innovate>

auditors who provide assistance in carrying out forensic audit of specific cases.

Further, SEBI has set up a dedicated cell called the “Connection Research and Analysis Cell” to unearth sophisticated connections, while investigating complex cases of insider trading and front running, by using innovative methods/ processes and digital tools/techniques.

ASIC has established an Office of Enforcement (OoE) to strengthen its enforcement effectiveness, decision making and capabilities, and executing its Enforcement Strategy. The OoE incorporates ASIC’s existing enforcement divisions and enables ASIC to have a single enforcement strategy, and to better prioritise the most important enforcement matters, promote stronger governance and oversight across enforcement functions, create flexibility in using enforcement resources, and build enforcement capability through training and the use of technology and data.

## **Prioritisation**

120. The prioritisation of cases and the allocation of enforcement resources is challenging in an environment of increasing regulatory scope and a constantly stretched resource base. To make more efficient use of resources, some regulators have implemented programmes which allocate resources to activities that pose the most risk to investors and the markets.

## **EXAMPLES**

Many regulators adopt a risk-based approach to enforcement - using risk assessment tools to analyse risk and then allocating resources to the most important problems. Co-ordination of risk and strategic intelligence analysis is critical to ensuring that priority is given to the risks likely to cause more harm to the financial markets and investors.

The NZ FMA also has a robust strategic intelligence operational model which places a strong emphasis on risk-based regulation. This ensures that the NZ FMA has the ability and infrastructure to identify the most important detriments facing the market and the ability to select the right tools to fix them. The collation and analysis of market and internal data and information to develop risk-based entity models are at the centre of the NZ FMA’s approach to regulation including enforcement activities. Business analysts from the strategic intelligence unit work along-side the enforcement team to ensure that data and information is taken into account in enforcement activities and the setting of priorities.

The US CFTC Division of Enforcement employs a staged approach to investigations beginning with a triage function in which a preliminary analysis is conducted for each referral or lead to determine whether it merits closer scrutiny. As a matter progresses through each stage, the Division undertakes regular reviews to consider significant factual and legal issues and assess the viability of particular matters to ensure the efficient allocation of resources.

The Case Intake Team of the HK SFC ensures that the Enforcement Division is focused on addressing the most serious threats to Hong Kong’s financial markets. When a case is referred to the team, it looks at:

- the facts and circumstances and weighs its importance according to the Enforcement Division’s current regulatory priorities;
- whether there is enough information to take the case further; and
- whether the problem is part of a larger issue.

A recommendation would then be made to the senior management of the division. If the senior management considers an investigation is warranted, it will allocate the case to one of its

specialised enforcement teams.

121. Having access to data and metrics can enable regulators to better determine priorities. Once priorities are determined then enforcement strategies can be designed and implemented. Several regulators have established research units to collate and analyse such information. Complaints, and surveillance databases and programmes are useful sources of information.

### Capacity

122. Regulators are increasingly asked to do better with less resources.

123. Credible deterrence is difficult to achieve without a foundation of appropriate levels of funding and access to:

a.) skilled and experienced staff;

b.) intellectual capital to keep abreast of financial innovation; and

c.) innovative technology and practices to allow regulators to fulfil their mandates.

124. Resourcing within regulators should recognise the value of retaining appropriately qualified and skilled staff.

125. Several assessments, including those carried out by the International Monetary Fund (IMF)<sup>58</sup>, have identified that underfunding of regulators is a significant impediment to the effectiveness and credibility of regulatory and enforcement programmes. Underfunding diminishes the capacity of regulators to deploy resources and staff who are sufficiently skilled and experienced to meet the challenges of contemporary regulation and hinders the capacity of regulators to prosecute successful cases that enhance credible deterrence.

### Strategy

126. The globalisation of finance and business has made unilateral approaches to enforcement less effective in some circumstances. To be effective and to deter misconduct, regulators require the capacity to regulate domestic and transnational transactions and business activities. To achieve this, regulators should consider developing relationships and strategies with domestic, national, and global authorities. Regulators should consider having a broad but well-defined remit, supplemented by robust domestic powers and extraterritorial practices to enable regulators to respond to the globalisation of misconduct.

127. Strategies should aim to prevent misconduct, reduce the cost of regulation and augment deterrence programmes. Strategies that encourage voluntary compliance with obligations can be as, or more, effective than strategies based on enforcement and punishment alone. Regulators should therefore consider both proactive and reactive programmes, and how to maximise efficient communication and cooperation between those in each programme.

### EXAMPLES

The HK SFC adopts a front-loading approach to its regulation. It places emphasis on early and more targeted intervention to nip problems in the bud. This means delivering fast and responsive regulation to maximise the impact of enforcement actions. It also focuses on the greatest threats, or the most significant or systemic risks in the market. The Enforcement Division has changed how it organises itself to be more specialised, collaborative, and multi-disciplinary, making much better use of its resources.

---

58 The IMF administers the Financial Sector Assessment Programme, a comprehensive and in-depth analysis of a country's financial sector.

The HK SFC has set up special operational teams drawn from different divisions to take on the more entrenched and serious market problems. One of these, codenamed “ICE”, pools senior level expertise from its Intermediaries, Corporate Finance and Enforcement divisions in a concerted effort to tackle problems ranging from sub-standard IPO sponsor work to untoward volatilities in the Growth Enterprise Market, to complex corporate cases. The combination of expertise and resources has allowed the HK SFC to undertake larger and more focused actions in response to a wider range of threats.

## Innovation

- 128.** Financial and technological innovation has made it increasingly challenging for regulators to track and keep pace with transactional information flows and financial products and services which are increasingly complex, specialised, and global. Regulators can continue meeting the challenges of the market by:
- a.) keeping pace with market innovation;
  - b.) identifying and resolving regulatory vulnerabilities;
  - c.) deploying effective enforcement strategies; and
  - d.) developing intellectual and technological capacities.
- 129.** Forward looking regulators can look outside the field of enforcement to identify innovative practices that can be used to enhance deterrence, maintain the currency of their understanding of new financial products and technology, and liaise with international counterparts to share ideas and innovative practices.

## Specialised enforcement tools

- 130.** A range of tools are available to help regulators achieve credible deterrence. For example, innovative research and planning tools to properly plan and manage enforcement activity, including through forecasting and market studies. Regulators should also consider using the latest market monitoring software to detect market misconduct. Furthermore, electronic tools such as digital forensic technology and e-discovery<sup>59</sup> may assist investigations and prosecutions.
- 131.** It is the combination of regulatory strategy, tools, and resources rather than any one part which determines the overall effectiveness of securities enforcement. To remain with, or ahead of, prevailing unlawful practices, regulators can regularly review their enforcement strategies and practices and retool their kits with innovative and effective powers. Factor 4 - Comprehensive Powers - contains examples of some useful powers some jurisdictions have applied to remediate and sanction illegal conduct.

## EXAMPLES

Many investigations, in particular complex cross-border investigations, frequently involve the urgent processing of complicated evidence and information in electronic files. Information and documents obtained from persons under investigation often have to be uploaded onto regulators' internal evidence management systems. To make this quicker and more efficient, the UK FCA has developed a standard template and standard data formats which are used when requesting documents and information. The UK FCA also liaises closely with entities under investigation to ensure that the data is provided in the right format and to agree workarounds where this is not

---

<sup>59</sup> E-discovery is an abbreviated term for electronic discovery. It is the obligation of parties engaged in legal proceedings to exchange documents that exist only in electronic form.

possible.

Many regulators now use risk assessment tools to measure and monitor risk in entities under their supervision. Some regulators also use robust investigation planning processes built upon the framework of project management methodologies.

SEBI has put in place a *Data Warehouse and Business Intelligence System* (DWBIS), which involves extensive use of the latest data warehousing and business intelligence technologies to support a far wider range of capabilities (including historical data analysis, transaction-based reporting, trading pattern recognition, fraud detection and establishing connections among clients). DWBIS comprises data warehouse, data mining and business intelligence tools. This upgraded surveillance mechanism implemented by SEBI is intended to effectively supervise market activities in a comprehensive manner.

The US CFTC typically provides “Data Delivery Standards” with requests for documents or data to facilitate the receipt of complete productions that are compatible with the agency’s technology<sup>60</sup>. An in-house team of information technology specialists ensures that access to evidence produced to the Division is limited to authorised personnel and works with staff to employ tools and strategies to efficiently and effectively review high volume productions. The US CFTC’s Division of Enforcement uses a comprehensive data analytics platform to quickly identify critical facts and the relevant context. The Division’s ability to use these tools, in combination with the Commission’s enhanced access to and analysis of trading and market data, allows staff to comprehend the activities quickly and thoroughly under investigation.

The US SEC Enforcement Division includes multiple specialised units and task forces which help provide additional structure, resources, and expertise necessary for enforcement staff to keep pace with ever-changing markets, and more comprehensively investigate cases involving complex products, markets, regulatory regimes, practices, and transactions.

The US SEC has also developed HAL—the High-Frequency Analytics Lab—to enhance the SEC’s capabilities in examinations and oversight of market microstructure including high-frequency trading. HAL produces reports on SEC registrant and market behaviour at the relevant time with resolutions down to microseconds. These reports help to identify registrants engaging in potentially unfair market practices, and to shed light on major market events<sup>61</sup>.

Laws requiring regulated entities to report suspected misconduct to ASIC have been recently strengthened, with a lower threshold obligation to breach report. ASIC is adopting a technology assisted approach to analyse these breach reports (which are expected to increase in volume) to more quickly identify significantly harmful and potentially systemic misconduct.

CONSOB is continuing to innovate its IT systems, processes and tools as part of its strategy to support the digital evolution of its supervisory and enforcement activities. Initiatives underway include the addition of new information sources and of a smart dashboard to its data warehouse, the creation of a data lake to share supervisory data, the use of text mining techniques to analyse documents received from supervised entities, and the application of artificial intelligence to facilitate the timely detection of unauthorized offers of financial products and market manipulation.

The OSC's Enforcement Branch (EB) is currently supported by a dedicated Electronic Discovery and Analytics (ED&A) unit which delivers a catalogue of multiple services across six distinct

---

60 <https://www.cftc.gov/LawRegulation/Enforcement/EnforcementManual.pdf>

61 Chairman Jay Clayton, Keynote Remarks at the Mid-Atlantic Regional Conference, June 4, 2019, available at <https://www.sec.gov/news/speech/clayton-keynote-mid-atlantic-regional-conference-2019>

competencies; namely: Vaulting, Digital Forensics, Electronic Discovery, Advanced Analytics, Open-Source Intelligence (OSINT) and a full-service Copy Centre. The unit is staffed by technical specialists carrying niche law enforcement and online intelligence expertise. They support the EB's core investigatory, regulatory, and prosecutorial mandate, carrying out evidence collection, analysis, disclosure and production obligations in investigations and litigation, by leveraging industry leading eDiscovery and digital forensics technology, cutting edge Data Science solutions, and disruptive OSINT tradecraft on emerging financial market, crypto/digital asset and social media engineered threats.

### Measuring effectiveness

132. Regulators who measure and publicise reports about their performance can enhance public understanding of their objectives and effectiveness. It is common practice for regulators to publish reports about their enforcement programmes. The metrics used to assess and measure effectiveness differ among regulators. Some common quantitative metrics include the number and type of investigations completed, prosecutions filed, persons sanctioned and amount of sanctions imposed.
133. By their nature, qualitative measures, such as whether enforcement action has improved market behaviour, are difficult to perform. Even when a regulator might perceive that it is achieving credible deterrence and changing behaviour, it can be difficult to identify whether enforcement action is the principal causal factor or whether there are other factors at play. Regulators are trying to develop more sophisticated measures to improve their effectiveness, and plan strategies for the future (sometimes known as second generation metrics).
134. Some ideas for measures that go beyond simple output metrics and attempt to measure strategic effectiveness are suggested below. Regulators may wish to consider whether these measurement tools add insight and value to their deterrence efforts.
  - a.) Observable data: This practice involves the analysis of trends in behaviour by observing and measuring what happens in the markets. For example, market cleanliness statistics count the number of potential suspicious market transactions that occur immediately before a company announcement and compare that data to actions against market abuse or insider dealing taken by the regulator. Another example is the number of audit reports qualified for client money reasons.
  - b.) Feedback: This practice involves gathering feedback from stakeholders on credible deterrence and changing behaviour it is essentially asking people how the regulator is doing. Collecting feedback can be done in a number of ways, such as by questionnaires and surveys, in meetings and conferences, directly or through advisors or lawyers or groups or panels, as part of the supervisory or enforcement process, or by tapping into former regulators who have gone out into industry.
  - c.) Media mining: This practice involves the use of sophisticated analytical tools to measure media reaction in both traditional and social media. The measurement is not limited just to column inches but also assesses whether the reaction is favourable (that is, whether it is supportive, or whether the regulator's key messages have been understood).
  - d.) Econometric modelling: This discipline is a forecasting technique that uses mathematical equations and statistics (based on historical data and/or relevant assumptions) to predict future economic conditions. This then helps help direct marketing or communications spending to where it will have most impact. This modelling can also be used to determine the economic impact of enforcement actions and policies.

135. IOSCO's *Key Elements in the Assessment of an Effective Enforcement Programme*<sup>62</sup>, identifies some criteria by which the effectiveness of enforcement programmes may be assessed.

## EXAMPLES

The UK FCA's Enforcement and Financial Crime Division offers feedback meetings to those who have been the subject of a concluded regulatory (but not criminal) investigation. The purpose of the feedback meeting is not to discuss the merits of the case or the outcome of the investigation, but to explore how the enforcement process has worked. The feedback meetings are also used to ask questions about the impact of the enforcement action on the entity or person concerned, such as whether they have put in governance, systems, or process improvements as a result of the enforcement action, and the impact of other enforcement actions, such as whether enforcement Final Notices are discussed in compliance meetings or at Board level. The reports of these meetings are used to consider whether any changes should be made to enforcement's processes or strategy and are reported in anonymous summary format in the UK FCA's Enforcement and Financial Crime Annual Performance Account.

The US SEC's Division of Economic and Risk Analysis uses analytical approaches, methods, and models in order to identify trends, risks or potential securities law contraventions in the capital markets.

The US CFTC's Division of Enforcement has released annual reports providing the public with several important metrics such as the number of enforcement actions filed, the amount of monetary sanctions imposed, and the number of actions filed in cooperation with criminal authorities or other regulators. Such reports also include information about significant matters, current enforcement priorities, and strategic initiatives<sup>63</sup>. The agency also issues a number of other periodic reports which include budget and performance data such as the Agency Financial Report, the President's Budget, and the Annual Report on the Whistleblower Program and Customer Education Initiatives, which are available on the agency's website<sup>64</sup>.

SEBI publishes an annual report containing details of all enforcement actions undertaken during the previous 12 months. Such reports are made publicly available. The reports contain data with respect to enforcement orders which were upheld and set aside by judicial forums.

The Australian Government has introduced legislation and established the Financial Regulator Assessment Authority, an independent authority, which is required to undertake regular review and oversight of ASIC (and also the Australian Prudential Regulatory Authority - APRA) and assess the performance and effectiveness of both regulators.

In March 2006, the UK Financial Services Authority (now UK FCA) issued Occasional Paper 23 Measuring Market Cleanliness which proposed measures of market cleanliness based on the extent to which share prices move ahead of the regulatory announcements that issuers are required to make to the market. The paper examined two broad kinds of announcement: those relating to take-over bids; and those about the trading performance of FTSE350 listed issuers. The UK FCA examined whether movements that were abnormal compared to a stock's normal movement might reflect insider trading. The UK FCA now publishes these statistics annually.

The UK FCA publishes an Enforcement Annual Performance Account (APA) at the same time as its Annual Report and Accounts every year. The APA looks at the fairness and effectiveness of

<sup>62</sup> Non-public Report of IOSCO Committee 4 for Enforcement and the exchange of Information, (IOSCO member's only webpage).

<sup>63</sup> [https://www.cftc.gov/media/5321/DOE\\_FY2020\\_AnnualReport\\_120120/download](https://www.cftc.gov/media/5321/DOE_FY2020_AnnualReport_120120/download)

<sup>64</sup> <https://www.cftc.gov/About/CFTCReports/index.htm>

the UK FCA's enforcement function over the financial years and summarises the activities and achievements of the enforcement function in the previous 12 months. It also considers feedback from entities that have been investigated and lessons learned from investigations so as to continually enhance and improve the enforcement function. publishes these statistics annually.

### Understanding behaviour

136. Deterrence in securities regulation can be maximised when regulators understand the drivers of good and bad behaviour and design regulatory programmes (such as enforcement) to incentivise and sanction such behaviours respectively.
137. Behavioural economics is an innovative tool which enables regulators to better understand the factors that influence investor decisions and the drivers of the behaviour of all market participants. Such insight may prove helpful in the early identification of risks and discourage certain risky and/or wrong practices employed by entities.

### EXAMPLES

The UK FCA uses behavioural economics to understand changing investor behaviours, and in so doing aims to intervene in markets more effectively, and in new ways, to counter inappropriate business models and to secure better outcomes for investors<sup>65</sup>. It has also conducted research into how to encourage consumers who may be due redress to respond to letters from financial firms concerning redress exercises. This has involved using behavioural economics to improve the drafting of such letters in order to ensure the highest possible response rate.

---

65 See the discussion in the UK FCA's Occasional Paper No.1 *Applying Behavioural Economics at the Financial Conduct Authority*, April 2013, available at <http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-1>  
See the discussion in the UK FCA's Occasional Paper No.2 - *Encouraging consumers to claim redress: evidence from a field trial* available at <http://www.fca.org.uk/your-fca/documents/occasional-papers/occasional-paper-2>

## Bibliography

- Ana Carvajal and Jennifer Elliott, *The Challenge of Enforcement in Securities Markets: Mission Impossible?* IMF Working Paper No. 09/168 2009.
- Ana Carvajal and Jennifer Elliott, *Strengths and Weaknesses in Securities Market Regulation: A Global Analysis*, IMF Working Paper No. 07/259 2007.
- Australian Securities and Investments Commission: *Sustaining a Credible Deterrence Framework: An ASIC report to Standing Committee 4 of the IOSCO Technical Committee*, June 2013.
- Australian Securities and Investments Commission: *Report 387, Penalties for Corporate Wrongdoing*, March 2014.
- Confidential Report of Standing Committee 4 of the Technical Committee of IOSCO, *Key Elements in the Assessment of an Effective Enforcement Programme*, May 2012.
- Eddy Wymeersch, Klaus J. Hopt and Guido Ferrarini, *Financial Regulation and Supervision: A Post-Crisis Analysis*, Oxford University Press, 2012.
- ESMA, *Report: Actual Use of Sanctioning Powers under MAD*, ESMA/2012/270, 26 April 2012.
- European Commission, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Reinforcing Sanctioning Regimes in the Financial Services Sector*, COM (2010) 716 final, 8 December 2010.
- Helen Bird, Davin Chow, Jarrod Lenne and Ian Ramsay, *Research Report: ASIC Enforcement Patterns*, Centre for Corporate Law and Securities Regulation, The University of Melbourne, 2003.
- IIF Regulatory Affairs, *Report: Promoting Greater International Regulatory Consistency*, June 2013. IOSCO, *Objectives and Principles of Securities Regulation*, June 2010.
- IOSCO, *Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation*, September 2011.
- Karen Yeung, *Quantifying Regulatory Penalties: Australian Competition Law Penalties in Perspective*, 23 Melbourne. U. L. Rev. 440, 1999.
- Kyla Malcolm, Mark Tilden, Scott Coope and Charlie Xie, *Assessing the Effectiveness of Enforcement and Regulation*, CRA International, April 2009.
- OECD, *Principles for the Governance of Regulators: Public Consultation Draft*, 21 June 2013. Remarks by David Wright to the Atlantic Council, Washington, DC, 10 December 2012.
- Ziven Scott Birdwell, *The Key Elements for Developing a Securities Market to Drive Economic Growth: A Roadmap for Emerging Markets*, Georgia Journal of International & Comparative Law, Spring, 2011.

#### **Committee 4 Members**

Comisión Nacional de Valores, **Argentina**  
Australian Securities and Investments Commission, **Australia**  
Securities Commission of the Bahamas, **Bahamas**  
Financial Services and Markets Authority, **Belgium**  
Comissão de Valores Mobiliários, **Brazil**  
British Columbia Securities Commission, **British Columbia**  
China Securities Regulatory Commission, **People's Republic of China**  
Dubai Financial Services Authority, **Dubai**  
Autorité des marchés financiers, **France**  
Bundesanstalt für Finanzdienstleistungsaufsicht, **Germany**  
Hellenic Republic Capital Market Commission, **Greece**  
Guernsey Financial Services Commission, **Guernsey**  
Securities and Futures Commission, **Hong Kong**  
Securities and Exchange Board of India, **India**  
Israel Securities Authority, **Israel**  
Commissione Nazionale per le Società e la Borsa, **Italy**  
Securities and Exchange Surveillance Commission, **Japan**  
Financial Services Agency, **Japan**  
Financial Services Commission/Financial Supervisory Service, **Korea, Republic of**  
Comisión Nacional Bancaria y de Valores, **Mexico**  
The Netherlands Authority for the Financial Markets, **The Netherlands**  
Financial Markets Authority, **New Zealand**  
Securities and Exchange Commission, **Nigeria**  
Ontario Securities Commission, **Ontario**  
Polish Financial Supervision Authority, **Poland**  
Comissão do Mercado de Valores Mobiliários, **Portugal**  
Autorité des Marchés Financiers, **Québec**  
Monetary Authority of Singapore, **Singapore**  
Financial Sector Conduct Authority, **South Africa**  
Comisión Nacional del Mercado de Valores, **Spain**  
Securities and Exchange Commission of Sri Lanka, **Sri Lanka**  
Swiss Financial Market Supervisory Authority, **Switzerland**  
Capital Markets Board, **Türkiye**  
Financial Conduct Authority, **United Kingdom**  
Commodity Futures Trading Commission, **United States of America**  
Securities and Exchange Commission, **United States of America**  
**IOSCO General Secretariat, MMoU Team.**