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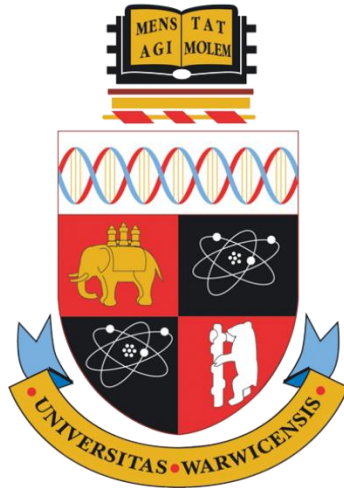
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# **Regulation and Supervision of Kuwait Capital Markets:**

## **A Critical Analysis of the Risk Based Approach**



By

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Thesis submitted in partial fulfilment of the requirements for the degree of  
Doctor of Philosophy in Law

School of Law

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Lastly, thank you to Allah to provide me with the strength and will to complete my PhD. Alhemallah.

This thesis submitted during the Coronavirus crisis; may Allah save the world.



### **Declaration**

This work is submitted to the University of Warwick in support of my application for the degree of Doctor of Philosophy. Except where acknowledged, this thesis is my original work. An early version of the Enforcement chapter has been published as an article in special issue of the Kuwait International Law School Journal in 2018.

## **Dedication**

I would like to dedicate my thesis to the memory of Grandmother **Lulwa Ali Al Tabtabaee**  
You will always be in my prayers.

## **Abstract**

Regulation of the financial markets requires a clear plan articulating how to financial regulators will allocate limited resources to highest risk areas. Each financial regulator has bring their own cultural views to the job of protecting the integrity of the markets. This research investigates Kuwait Capital Markets Law No.7 of 2010 and its effectiveness in providing adequate supervision and enforcement to prevent insider trading. Using a risk-based approach allows efficient analyses of the available data. Creating a new, risk-based framework to address the regulation of Kuwaiti capital markets and to formulate financial regulations that are sufficient and appropriate is an efficient and productive approach to much-needed regulatory reform. It also compares the Kuwaiti approach with the UK approach and IOSCO standards to reveal the weaknesses in Kuwait legal system. With these weaknesses in mind, better regulations to protect the markets can be promulgated. Elite interviews have been conducted in this research to fill gaps in the literature and review and validate the research findings. This research investigates the peculiar concomitant independence and accountability of Kuwait Capital Market Authority (CMA) and its mandate to be a robust regulator and to supervise and enforce regulations. In addition to the currently insufficient framework regarding disclosure obligations, the ill-defined legal responsibilities of insiders and inadequacies of the whistle-blowing system are among the notable shortcomings. This thesis also investigates enforcement procedures in financial services and stock markets. Taken together, there currently exist significant problems with the current framework that hinder the achievement of the CMA's goal to protect market integrity, prevent insider trading, and promote investor confidence. The resulting analyses herein suggest that insider trading regulations are inadequate to either deter or punish insider trading in the stock markets. As the CMA has not introduced a coherent risk-based approach to assess insider trading risks; that has become the main contribution of this work. This thesis discusses in-depth these flaws and proposes a variety of solutions and areas of improvement to develop a robust and effective scheme to regulate and deter the insider trading. It provides guidelines for the CMA to apply a risk-based approach to revising and implementing the new and necessary regulatory reforms.

## **Abbreviations**

ARROW      advanced regulatory risk operating framework

BFS    Barings Futures Singapore

BoE    Bank of England

CBK    Central Bank of Kuwait

CIO    chief investment officer

CJA    Criminal Justice Act 1993 (UK)

CMA    Capital Markets Authority (Kuwait)

CML    Capital Markets Law 2010 (Kuwait)

CSC    Civil Service Commission (Kuwait)

DEPP    Decision Procedure and Penalties Manual

DTRs    Disclosure and Transparency Rules

FCA    Financial Conduct Authority (UK)

FSA    Financial Services Authority (UK)

FSMA    Financial Services and Markets Act 2000 (UK)

IMF    International Monetary Fund

IOSCO    International Organization of Securities Commissions

KCC    Kuwait Clearing Company

KCL    Kuwait Criminal Law 1960

KSE    Kuwait Stock Exchange

MOCI    Ministry of Commerce and Industry (Kuwait)

MoU    memorandum of understanding

MP member of parliament

OECD Organisation for Economic Co-operation and Development

PIDA Public Interest Disclosure Act 1998 (UK)

PRA Prudential Regulation Authority (UK)

RATE risk assessment, tools and evaluation

RBS Royal Bank of Scotland

RDC Regulatory Decisions Committee (UK)

STOR Suspicious Transaction and Order Report (UK)

TBTF too big to fail

## Chapter 1: Introduction

### 1. Research context

Over the past few years many countries have experienced financial crises. This has generated considerable debate about financial supervision and enforcement regulatory reform. Kuwait was among the economies affected by the 2007–2008 financial crisis. While the crisis had multiple causes, arguably a major contributing factor was the absence of action by supervisory authorities who failed to take the steps necessary to avoid the crisis.<sup>1</sup> Gaps between the areas regulated by supervisory authorities combined with overlaps and institutional structures that unnecessarily duplicated regulatory responsibilities to hinder effective crisis management.<sup>2</sup> Enforcement of existing laws was absent resulting in little or no deterrence for those who acted outside the bounds of good judgment.<sup>3</sup> Enforcement ensures that regulated firms and licensed persons in financial services and stock markets act within the law and protects the market from the consequences of misconduct.<sup>4</sup> Moreover, scholars have since detected weaknesses in the overarching financial structure, including poor information gathering, lack of supervision, macro-economic instability, and inadequate regime management.<sup>5</sup> Lack of information to investors in stock markets is a primary contributor to insider trading. An International Monetary Fund (IMF) report in April 2019 identified the gaps in Kuwait's capital market regulatory framework and urged a shift from the current supervision approach towards risk-based supervision.<sup>6</sup> The report stressed the importance of installing financial regulators with clear micro-prudential and macro-prudential remits to prevent future financial crises.<sup>7</sup>

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<sup>1</sup> International Monetary Fund, 'Kuwait: Financial System Stability Assessment – Update' (Report No. 10/239, 24 July 2010) <<https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Financial-System-Stability-Assessment-Update-24096>> accessed 18 March 2020.

<sup>2</sup> *ibid.*

<sup>3</sup> We refer to the Enforcement Law as the tool and power that the financial regulator possesses to enforce law. Enforcement includes inspection, investigation and disciplinary action.

<sup>4</sup> Hussain Boaruki, *The Legal Protection for Capital Market Authority: Case Study of Kuwait and France* (Dar Alnahtha AlArbia 2016) 503; also see Abdullah Alshebli, 'The Protecting Individual Investors under Kuwaiti Securities', (PhD thesis, University of Leeds 2015) 127-130. and Fatima AlShuraian, 'Market Manipulation In - Kuwait Stock Exchange' (PhD thesis, University of Leicester 2013) 202.

<sup>5</sup> Eddy Wymeersch, Klaus J Hopt and Guido Ferrarini, *Financial Regulation and Supervision. A Post-Crisis Analysis* (Oxford University Press 2012) 486.

<sup>6</sup> International Monetary Fund, 'Kuwait: Financial System Stability Assessment – Update' (Report No. 19/96, April 2019) 4 <<<https://www.imf.org/en/Publications/CR/Issues/2019/04/02/Kuwait-Financial-System-Stability-Assessment-46730>>> accessed 21 January 2020.

<sup>7</sup> Dalvinder Singh and John Raymond Labrosse, 'Developing a Framework for Effective Financial Crisis Management' (2011) OECD Journal: Financial Market Trends, 4.

Since the 2007–2008 financial crisis, stock markets insider trading has captured the attention of Kuwaiti regulators concerned about the ongoing threat to market fairness and integrity. Insider trading can be defined as ‘the unfair use of material, non-public information concerning an issue of securities [which] threatens to undermine the integrity of the national securities markets.’<sup>8</sup> Prior to 2010, the Kuwait stock market suffered from insider trading due to insufficient regulation;<sup>9</sup> the only legislation preventing the use of inside information was Article 140 of Law No. 15 of the Companies Act of 1960, which concerned company law and only applied to boards of directors. This article was ineffectively vague and could not be implemented in practice, allowing significant inside dealing to take place prior to the introduction of new legislation in 2010.<sup>10</sup>

On 30 January 2017, the Kuwait government announced their vision to transform Kuwait into a financial and trade hub, attractive to investors, to diversify the economy away from oil by 2035.<sup>11</sup> Fulfilling this vision requires effective regulations to protect the market integrity and attract new investors. Insider trading represents a threat to this goal. Investors want to be informed about the state of the markets they invest in, thus a disclosure regime needs to provide adequate and fair information to all investors.<sup>12</sup> Developing and improving supervision and enforcement is a necessary step to establishing a stable financial sector.

Kuwait has adopted new policies to achieve financial regulators’ objectives. New financial law was introduced in the form of Capital Markets Law (CML) No. 7 of 2010, which was amended in 2014 and again in 2015.<sup>13</sup> This was the first time the Kuwaiti legal system created a new authority to supervise and regulate the non-banking financial sector. The CML establishes a legal framework for the financial markets’ supervisory authority, including the rules and

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<sup>8</sup> Oliver Colvin ‘A Dynamic Definition of and Prohibition Against Insider Trading’ (1991) 31 Santa Clara Law Review, 603, 633.

<sup>9</sup> Adel AlManea, ‘The Crime of Inside Trading and Using of Inside Information in Stock Markets: A Comparative Study Kuwait and France’ (2012) 37 Journal of Kuwait Law School 16, 34. See also Ahmed AlMulhem, ‘Insider Dealing in the Companies Act of Kuwait No.15 of 1960’ (1998) 3 Arab Law Quarterly 14, 33.

<sup>10</sup> The seven participants whom the researcher interviewed during the fieldwork agreed that there was insider dealing in the Kuwait stock market before 2010 and there was not sufficient regulation to prevent this practice.

<sup>11</sup> Kuwait New Summit available at << <https://newkuwaitsummit.com/>>> accessed 9 July 2020. Also see Oxford Business Group, ‘Kuwait’s economic strategy aims to deliver (2017) <<https://oxfordbusinessgroup.com/analysis/new-day-most-recent-ambitious-economic-strategy-aims-deliver-past-promises-and-new-goals>> accessed 9 July 2020

<sup>12</sup> Bernard Black, ‘The Core Institutions That Support Strong Securities Markets’ (2000) 55 Journal of Business Lawyer 1565, 1565-1566.

<sup>13</sup> ‘Capital Markets Law No. 7 of 2010 (CML)’ available at <<https://www.cma.gov.kw/en/web/cma/cma-handbook>> accessed 13 March 2020.

regulations under which the stock markets are organised and managed. After CML in 2010, additional legal framework for regulating insider activities was provided by Article 118 of the CML. In 2015, the Kuwait Capital Markets Authority (CMA) issued an amendment to the CML Executive Bylaws which explained all the financial regulations in detail.<sup>14</sup> Insider trading regulations were among the articles that were reformed in the 2015. Although the CML came into force almost a decade ago, there is still ample room to improve and develop financial regulations in Kuwait as discussed with this research.

In Kuwait, the three broad financial sectors, banking, insurance, and securities, are regulated separately. This thesis focuses solely on the securities sector, which is regulated by the CML, and examines the effectiveness of insider trading regulations in stock markets using a risk-based approach to analyse the available data. This research also focuses on the financial regulatory authority that supervises and enforces laws; comparisons between Kuwait and the approach taken by the UK and other international practices are used to identify pathway for reform.

In order to have effective insider trading regulations, the financial regulatory authority must be able to act independently, taking the necessary actions and making the decisions required to protect the public interest.<sup>15</sup> Political pressure can weaken financial oversight and hinder those charged with enforcing the law, preventing them from taking action regarding institutions that have run into trouble; for example, the financial regulatory authority may dismiss charges against a powerful listed firm with political influence over the regulators. It is important preserve the autonomy of financial regulators so that they may act on their mandate freely without external interference. In theory, the CML grants the CMA independence; in practice the CMA is not operationally free from external political or commercial interference. Experience has demonstrated that political interference in financial sector regulations leads to undesirable consequences.<sup>16</sup> Thus, to improve the quality of regulation and supervision with the ultimate goals of preventing financial crises and attracting new investors, it is essential to

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<sup>14</sup> Capital Markets Authority Kuwait, 'Executive Bylaws' (2015) <<https://www.cma.gov.kw/en/web/cma/-bylaw-documents>> accessed 13 March 2020.

<sup>15</sup> IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 8 July 2020.

<sup>16</sup> Eva Hüpkes, Marc Quintyn and Michael Taylor, *Accountability Arrangements for Financial Sector Regulators* (2006) International Monetary Fund, 13.



imbue the CMA with sufficient independence and autonomy so that it may effectively oversee a smoother and more efficient market operation.<sup>17</sup>

As a supervisory authority, the CMA possesses powerful tools to grant and withdraw licences; it must independently exercise these powers to protect the market without interference or undue influence. Hence there is a need to investigate any exertion of political or commercial influence and improve surveillance procedures to match those of other developed markets. Most economists believe that the independence of the CMA will enhance the long-term performance of the national economy.<sup>18</sup> At the same time, accountability for financial regulators must be incorporated to hold actors for their decisions and actions as an added layer of protection for financial services and stock market investors. Public accountability plays a major role in achieving the goal of a stable financial sector not reliant on oil and attractive to investors.

In the financial sector, there are two types of enforcement, public and private, each with its own characteristics.<sup>19</sup> In Kuwait, the CMA uses only the public method to enforce regulations.<sup>20</sup> The manner in which rules are enforced and compliance with financial regulations is ensured significantly influences investors' confidence in the market.<sup>21</sup> Mechanisms and tools of supervision include the right to investigate and assess reports and company records.<sup>22</sup> In order to uncover insider trading, the financial regulator must have be able to gather information from individuals and firms and an investigation may require a firm or individual to assist the inspector by answering questions. To compel cooperation, regulations punish noncompliance with the imposition of fines.<sup>23</sup> Additional information may be gathered by compelling the production of documentation from firms and individuals or via whistle-blowing reports. The ability to compel individual cooperation and document production along with the safe harbour of a whistle-blowing mechanism are important tools that enable financial

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<sup>17</sup> Marc Quintyn and Michael Taylor, 'Should Financial Sector Regulators Be Independent?' (2004) International Monetary Fund, available <<https://www.imf.org/en/Publications/Economic-Issues/Issues/2016/12/30/Should-Financial-Sector-Regulators-Be-Independent-16993>> accessed 13 March 2020.

<sup>18</sup> Chris Brummer, *Soft Law and the Global Financial System* (Cambridge University Press 2015) 30.

<sup>19</sup> Mark Roe and Howell Jackson, 'Public and Private Enforcement of Securities Law: Resource-Based Evidence' (2009) Harvard Law School John M. Olin Centre for Law Economic and Business Discussion Paper. Series. Paper 637. 14.

<sup>20</sup> Fatima AlShuraian, above, (n 4) 193.

<sup>21</sup> Dalvinder Singh, *Banking Regulation of UK and US Financial Markets* (Ashgate Publishing Limited 2007) 113.

<sup>22</sup> Madhar Farqli, 'The Criminal Protection of the Stock Market Trust: Stock Markets Crimes' (Cairo, Egypt, Dar AlNadhda AlArbia 2006) 461. See also Dalvinder Singh (n 21) 127.

<sup>23</sup> CML, Article 127.

regulator to prevent and address insider trading. These tools must, therefore, be well-protected to provide regulators with sufficient power to protect the markets.

The power to impose and enforce sufficient punishment for non-compliant firms and individuals is another substantial power to be granted to enable an effective regulatory regime. As part of their responsibilities, financial regulator must punish firms who do not disclose material information that might reveal insider trading. Punishments must be appropriate and sufficient to deter others from committing similar transgressions. Currently, there is an argument to be made that the CMA's enforcement powers and actions taken are insufficient in this area; punishment for non-compliance is applied to firms and individuals on an equal basis without taking into consideration financial dissimilarities between the two or acknowledging the disparate impact of subjecting individuals with relatively fewer resources to the same punishment as an entire firm.<sup>24</sup>

A previous study validated the need for sufficient sanctions to be available to regulators so the law can be enforced.<sup>25</sup> There are two approaches to law enforcement: encouraging compliance and deterring non-compliance, and the optimal approach is a combination of the two.<sup>26</sup> At this time, the Kuwaiti legal system has adopted something of command-and-control approach. This approach needs further investigation, and the best way for the Kuwaiti legal system to amend its current laws to meet the requirements of well-developed, well-regulated financial services markets remains open to suggestions.

In order to prevent and address insider trading in stock markets, the disclosure obligation for listed companies must be sufficient and strong. Consistent with fundamental principles of fairness, the CMA plays an important role in the financial sector by supervising listed companies' disclosures to ensure that investors have equal access to information and to prevent insider trading. For disclosure within the stock markets to be effective, complete, and timely information must be available to the public. This raises the question of whether the CML

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<sup>24</sup> Mohammad Al-Mutairi, 'A Critical Assessment Of Regulation Of Insider Trading Under The Kuwait Capital Market Authority Law: A Comparative Study With The Regulatory Structure Of The United State, The United Kingdom and France to Enhance Market Fairness, Integrity and Effective Enforcement Of The Kuwait Regulatory Structure' (PhD thesis, Case Western Reserve University 2018) 152.

<sup>25</sup> Fatima AlShuraian, above, (n 4) 190-193.

<sup>26</sup> Dalvinder Singh, 'The Centralisation of European Financial Regulation and Supervision: Is There a Need for a Single Enforcement Handbook?' (2015) 16 European Business Organization Law Review 439, 465.

defines ‘disclosure of information’ in terms clear enough to ensure the integrity of the disclosure system.

Information disclosure protects the markets from insider trading by giving investors equal access to information. Precisely for this reason, many jurisdictions have reformed their disclosure regulations to ensure that disclosure requirements contribute to the essential duties of regulators: to protect market integrity and prevent insider dealing. Thus, there is also a need to investigate the effectiveness of the disclosure regime in the Kuwait stock market and the CMA’s ability to supervise listed companies’ disclosures.

Insider trading in stock markets is one of the most sophisticated crimes in the financial sector with a profound effect the perceived integrity of markets. Insufficient disclosure requirements and a lack of supervision allows insiders to benefit from ineffective laws and regulations to engage in inside trading and self-dealing. To ensure a strong stock market that can attract new investors, it is extremely important to investigate the effectiveness of the current structure of laws and regulations governing the Kuwait stock market and evaluate the CMA’s capacity to effectively suppress insider trading. The primary question this chapter will investigate is whether the current criminal procedures and laws are enough to protect market integrity.

Whistle-blowing systems are a well-known method of uncovering insider dealing, but no previous studies have investigated the effectiveness of this system in Kuwait, so there is little understanding the efficacy of the whistle-blowing framework such as encouragement or reward incentives, the protections provided to whistle-blowers, and how the Kuwaiti culture may influence stock market whistle-blowing.

A fundamental problem addressed in this thesis is the fact that the CML was adopted from other jurisdictions without a proper understanding of the ancillary legal structures necessary for effective deployment.<sup>27</sup> For example Kuwait has adopted a criminal regime from UK to tackle and prevent insider trading without concomitantly adopting a civil regime similar to that in the UK which provides different and additional layers of protection. The problems with

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<sup>27</sup> Two of the participants who were interviewed by the researcher confirmed that CML No.7 of 2010 has been adopted from other jurisdictions. IOSCO, ‘Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries’, (2009) 3 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>> accessed 13 March 2020.

launching a displaced system need to be evaluated to explore weaknesses of the CML and suggest amendments.

The key question examined herein is whether the CMA effectively enforces its mandate to prevent insider trading through regulations and enforcement tools using risk-based approach to regulation. To answer this question, six factors are used to analyse the CML and its Executive Bylaws in terms of their effectiveness in regulating financial services and preventing insider trading.

The first factor is the independence of the CMA, which enables it to regulate financial services and stock markets, and the accountability of the CMA requiring regulators to account for any unreasonable decisions.

The second factor involves the appropriateness of the tools and powers that the CMA as supervisory authorities have to enforce the law. Enforcement powers provide financial regulators with tools to punish non-compliant individuals and firms serve as a deterrent to those who would engage in improper trading actions.

The third factor is the effectiveness of the disclosure regime in preventing insider trading in the Kuwait stock market. Control over information dissemination is the cornerstone of insider trading in any stock market; thus, if the disclosure regime is sound and solid, it should prevent criminal trading activities.

The fourth factor is the clarity of regulations and the effectiveness of their application by the legal system in terms of preventing insider trading. The legal framework used to establish oversight is important for effective regulation, particularly since Kuwait uses a criminal regime to regulate insider trading without adopting additional support from the realm of civil law; any lack of clarity places limits on efforts to prevent criminal activity.

The fifth factor involves the presence of a proper whistle-blowing framework to encourage individuals in the best position to observe illegal activities to come forward and report crimes.

The sixth and final factor is the clarity of the CMA's policies in terms of its ability to implement appropriate strategies to supervise and enforce financial regulations.

## 2. Background of Kuwait Capital Markets Law

The CML is the main focus of this research, therefore it is useful to explore the process and circumstances that led National Assembly to the issue the CML No.7 of 2010. Over the past few decades Kuwait has faced several difficulties, including the global financial crisis, which have led to the need for laws to organise the non-banking sector. The first such instrument was Law No. 35 of 1983, which dealt with regulating the Kuwait stock market. The law was a reaction to the financial crisis (*Almanakh*) of 1982. However, there were shortcomings in the legal framework, and thus on 27 December 1986 another law was passed to organise stock market trading and the clearing company for the Kuwait stock market.<sup>28</sup> From 1983 until the issuance of the CML No. 7 in 2010, these two laws regulated the stock market in Kuwait.

The CML began as a proposal by a member of parliament (MP) in 2004 to establish a 'Stock Market Authority'.<sup>29</sup> There were several reasons behind the proposal: the unregulated stock market, an increasing number of listed companies in the stock market, the transfer of shares from the public to the private sector, the overall lack of a legal framework governing the Kuwait stock market to protect investors<sup>30</sup> and the 2008 financial crisis.<sup>31</sup> Another major reason for issuing a law to regulate non-banking sectors stemmed from reports by international organisations that had evaluated Kuwait's financial sector. In May 2004 the IMF issued a report comparing the effectiveness of Kuwait's capital market regulations with international standards, and found that the country's financial sector exhibited weak governance structures, especially those relating to the capital market regulator itself.<sup>32</sup> The IMF Financial System Stability Assessment team conducted assessments using three international standards and codes: the Basel Core Principles for Effective Banking Supervision; the Objectives and Principles of Securities Regulation; and the Anti-Money Laundering and Combating the Financing of Terrorism Standards. The IMF issued another report in November 2004 regarding compliance with the International Organization of Securities Commissions' (IOSCO)

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<sup>28</sup> Adel AlManea, above (n 9) 16, 44.

<sup>29</sup> Kuwait National Assembly, Session No. 1108/A, 1 November 2004.

<sup>30</sup> Jusic Asim and Yassen Farah, 'International Standards and the Administrative Model of Capital Market Regulation in Kuwait' (2016) 4 Kuwait International Law School Journal 17, 50.

<sup>31</sup> Participant No.3 from the conducted interviews.

<sup>32</sup> International Monetary Fund, 'Kuwait: Financial System Stability Assessment, Including Reports on the Observance of Standards and Codes on the Following Topics: Banking Supervision, Securities Regulation, Anti-Money Laundering and Combating the Financing of Terrorism', Report No. 04/151 (May 2004) <<  
<https://www.imf.org/en/Publications/CR/Issues/2016/12/30/Kuwait-Financial-System-Stability-Assessment-including-Reports-on-the-Observance-of-17423>> accessed 13 March 2020.

objectives and principles, which found that many of these principles had not been implemented.<sup>33</sup> According to the IMF reports, Kuwait had multiple authorities with unclear and overlapping powers regulating the financial service and stock markets, and all of these lacked operational independence and accountability when exercising their functions and powers.<sup>34</sup>

The recommendations set forth in these reports led to a significant debate between the National Assembly and the Council of Ministers, which continued for a couple of years until an agreement on best practices was reached; the debate ultimately culminated in the adoption of the CML. A brief overview of that process is set out here. Following the IMF reports, the Council of Ministers assigned the Minister of Commerce and Industry to carry out additional studies regarding the establishment of a CMA. On 23 January 2007 the minister declared that the draft of the Capital Markets Authority Law was in its final stages and ready to be delivered to the Council of Ministers, after which it would proceed to the National Assembly for final approval. The Council of Ministers referred the draft law to the Legal Advice and Legislation Department for consideration and final comments. On 11 June 2007 the chairman of the Committee on Economic and Financial Affairs submitted a letter to the president of the National Assembly requesting it to postpone the review of the bill until the next legislative term.<sup>35</sup> However, it took approximately three years to review and draft what eventually became the CML. In 2008 the global financial crisis and the collapse of the stock market forced the Council of Ministers and the National Assembly to exert greater effort to pass the CML.

The National Assembly of Kuwait issued Capital Markets Law No. 7 of 2010 (the **CML**) on 21 February 2010, establishing the CMA to supervise investment companies and investment funds as well as banks engaging in securities activities. However, under the CML the banking sector and investment companies that practise finance activities were to remain under the

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<sup>33</sup> International Monetary Fund, 'Kuwait: Financial Sector Assessment Program Detailed Assessments of Observance of Standards and Codes - International Organization of Securities Commission (IOSCO) Objective and Principles of Securities Regulation', Report No. 4/352, (2004) << <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Financial-Sector-Assessment-Program-Detailed-Assessments-of-Observance-of-Standards-17829>>> accessed 13 March 2020. See also Jusic Asim and Yassen Farah, above (n 30) 50

<sup>34</sup> Ibid. 2 and 50.

<sup>35</sup> Bader Alotaibi, 'Corporate Governance and Voluntary Disclosure in Kuwait' (PhD thesis, University of Bedfordshire 2014) 72.

supervision of the Central Bank of Kuwait (**CBK**).<sup>36</sup> The CML is considered the most complex law regulating the non-banking financial sector promulgated in the recent history of Kuwait,<sup>37</sup> and it soon became apparent that its enforcement needed to be facilitated by further regulation. Hence on 13 March 2013 the CMA's Council of Commissioners, implemented under CML Article 152, adopted Resolution No. 2-4 of 2011 to issue Executive Bylaws and publish them in the official gazette (*Kuwait Al-Yaum*).<sup>38</sup> The CML and its Executive Bylaws have since been amended several times to improve financial regulation; the latest amendments were made in Resolution No. 72 of 2015, issued in November 2015. The said resolution changed the previous Executive Bylaws with new 16 modules which describe all rules and regulations related to financial services and stock markets. Although these amendments are now in place, there is still room for improvement, as explored by this research.

### 3. Research questions

This research focuses on the issues discussed above to answer questions about financial services and stock markets.

The key question is as follows:

- Does the CMA have effective regulations to tackle and prevent insider trading in stock markets?

Secondary questions are listed below.

- What is the appropriate approach to financial markets regulation?
- Is the CMA sufficiently independent from governmental and parliamentary influence while still being legally accountable for its decisions and actions?

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<sup>36</sup> Zamir Mirakhor, *An Introduction to Islamic Finance* (2<sup>nd</sup> Edn John Wiley & Sons 2014) 261. See International Monetary Fund, 'Kuwait: Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism' (Report No. 11/268, September 2011) available <<  
<https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Detailed-Assessment-Report-on-Anti-Money-Laundering-and-Combating-the-Financing-of-25210>>> accessed 20 February 2020.

<sup>37</sup> Oxford Business Group, 'Kuwait's Banking Industry Looks to the Future' (2015) <  
<https://oxfordbusinessgroup.com/overview/solid-fundamentals-one-country's-most-stable-industries-looks-future>> accessed 21 January 2020

<sup>38</sup> Abdullah AlKharafi and Abdullah AlHaroun 'Kuwait' in Jeffrey Golden (ed), *The International Capital Market Review* (4th edn, Law Business Research 2016) 221. Article 152 of the CML provides the authority to the board of commissioners to issue executive bylaw.

- Does the CMA have the requisite powers and tools to deter and uncover detect crimes and violations in financial services and stock markets? Is the enforcement sufficient to deter and detect these crimes and violations?
- Do the CMA regulations establish a disclosure regime sufficient to prevent insider trading Is the legal framework that establishes and identifies insider trading clear?
- Is the whistleblowing system sufficient to encourage whistleblowers to reveal crimes?

#### **4. Aims and objectives**

The aims and objectives of this research are to explore and evaluate the following issues.

1. The application of risk-based approach to regulate insider trading and the clarity of the CMA's policies to supervise and enforce financial services and stock market regulation.
2. The legal framework governing the CMA in terms of its independence and accountability.
3. The legal framework for the enforcement and invocation of the CMA's supervisory powers.
4. Regulatory transparency to provide a sufficient legal framework for disclosure.
5. The clarity of regulations and their effectiveness in terms of preventing insider trading.
6. The role of whistleblowing regulations in encouraging individuals to come forward and disclose wrongdoing.

#### **5. Research methodology**

In social science research there are two main methods: quantitative and qualitative.<sup>39</sup> For the purposes of this study, the qualitative method was adopted to analyse primary and secondary sources. This method helps to meet a variety of objectives in any study.<sup>40</sup> It allows the analysis of the CMA's policies concerning financial regulation, particularly whether its risk-based approach is effective. It is important to evaluate the achievement of the regulatory objectives to assess the strengths and weaknesses of the regulatory regime and whether it is efficient in meeting its goals.

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<sup>39</sup> Matt Henn, Mark Weinstein and Nick Foard, *A Short Introduction to Social Research* (SAGE Publications 2006) 116.

<sup>40</sup> Jane Ritchie and Liz Spencer, 'Qualitative Data Analysis for Applied Policy Research' (2002) 573 *The Qualitative Researcher's Companion* 173, 176.



The qualitative method is defined as ‘any kind of research that produces findings not arrived at by means of statistical procedures or other means of quantification’.<sup>41</sup> The objective of this method is to understand people’s behaviour and thoughts by recording detailed descriptions of the issues;<sup>42</sup> it helps to understand processes and provides in-depth explanations of issues.<sup>43</sup> A good description of the qualitative method can be found in Hakim’s statement distinguishing between quantitative and qualitative research: ‘If surveys offer the bird’s eye view, qualitative research offers the worm’s eye view.’<sup>44</sup> The method gives insightful perspectives on the investigation, which helps to validate research findings.<sup>45</sup>

What qualitative research can offer the policy maker is a theory of social action grounded on the experiences – the world view – of those likely to be affected by a policy decision or thought to be part of the problem.<sup>46</sup>

In-depth, one-to-one interviews were used to conduct qualitative research and achieve research objectives. A discussion of the research methodology used for collecting and analysing the data is provided in Appendices 1 and 2 to this thesis. The interviews gave insights into problems and allowed the researcher to gain an understanding of underlying reasons and opinions, thus helping to develop the research. The project used semi-structured interviews with open-ended questions: the interview questions are noted in Appendix 3, and they were addressed to seven elite experts in the Kuwait financial sector, who made a significant contribution to this thesis. An outline of the elite qualifications and expertise of the interviewees is provided in the following paragraphs. It is important to note that the interviews focused on the Kuwaiti legal system in terms of the issues and problems that the experts face in practice.

It is useful to define comparative law and its function in this research. Comparative law is a method to compare two or more legal systems or parts, branches or aspects of two or more legal systems. According to Kamba’s methodology, there are two approaches to comparative law: macro-comparison and micro-comparison.<sup>47</sup> Macro-comparison is concerned with two or

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<sup>41</sup> Juliet Corbin and Anselm Strauss, *Basics of Qualitative Research* (Newbury Park, SAGE Publications 1990) 17.

<sup>42</sup> Matt Henn, Mark Weinstein and Nick Foard, above (n 39)149.

<sup>43</sup> Aashish Srivastava and S Bruce Thomson, 'Framework Analysis: A Qualitative Methodology for Applied Policy Research' (2009) 73.

<sup>44</sup> Catherine Hakim, *Research Design: Successful Designs for Social and Economic Research* (2nd edn Routledge 2000) 36.

<sup>45</sup> Robert Yin, *Case Study Research: Design and Methods* (5th edn SAGE 2003) 3-14.

<sup>46</sup> Walker, 1985:19 cited in Jane Ritchie and Liz Spencer, above (n 40) 4174.

<sup>47</sup> Walter Kamba, 'Comparative Law: A Theoretical Framework, (1974) 23 International and Comparative Law Quarterly, 485, 506.

more entire legal systems, whereas micro-comparison is limited to aspects or topics of two or more legal systems.<sup>48</sup> The choice of a specific financial supervision system depends on political, historical and path-dependent factors.<sup>49</sup> This research attempts to address the supervision and enforcement of market regulations and determine how the CML regulates CMA supervision and enforcement through a comparison with the power of the UK Financial Conduct Authority (FCA) under the Financial Services Act 2012. In the UK, financial regulation was set forth in the Financial Services and Markets Act 2000 (FSMA), which created a single regulator, the Financial Services Authority (FSA). In April 2013 the single regulator experiment ended, and two regulators were created: the FCA and the Prudential Regulation Authority (PRA) were both established by the Financial Services Act 2012.<sup>50</sup> This comparative law research can help suggest better solutions and regulations to govern the financial sector.

Comparative law is not a branch of national law.<sup>51</sup> It is well known that adoption of the term ‘comparative law’ can lead to misunderstandings or be misleading, but as Gutteridge points out, the term ‘has become so firmly established that it must be accepted, even if it is misleading’.<sup>52</sup>

However, there are many common problems in terms of the financial regulation of any country that can be solved using comparative law. It helps to highlight these common problems and suggest better regulations to overcome them.<sup>53</sup> The importance of comparative law lies in finding a solution that could benefit one jurisdiction by comparing two legal systems. As Kotz and Zweigert agree, the importance of comparative law is that ‘legislators all over the world have found that on many matters good laws cannot be produced without the assistance of comparative law’.<sup>54</sup> In fact, there are many advantages to using comparative law: as Kamba states, it ‘liberates one from the narrow confines of the individual systems. It is one of the most effective instruments for gaining a better knowledge and deeper understanding of one’s own

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<sup>48</sup> *ibid*, 506.

<sup>49</sup> Eddy Wymeersch, ‘The Structure of Financial Supervision in Europe: About Single, Twin Peaks and Multiple Financial supervisors’ (2007) 8 *European Business Organisation Law Review* 10

<sup>50</sup> Andreas Kokkinis, ‘Rethinking Banking Prudential Regulation: Why Corporate Governance Rules Matter’ (2012) 7 *Journal of Business Law* 612, 629.

<sup>51</sup> Kamba, above, (n 47) 7.

<sup>52</sup> Harold Cooke Gutteridge, *Comparative Law: An Introduction to the Comparative Method of Legal Study and Research* (1946) (CUP Archive) 1–2; also see Kamba, above, (n.47) 487.

<sup>53</sup> Terry Hutchinson, *Researching and Writing in Law* (2nd edn, Lawbook Co 2006) 106.

<sup>54</sup> Hein Kotz, and Konrad Zweigert, *An Introduction to Comparative Law*, vol. 2, Trans, (2<sup>nd</sup> Oxford University Press 1987) as cited in Jonathan Hill, ‘Comparative Law, Law Reform and Legal Theory’ (1989) 9 *Oxford Journal of Legal Studies*, 101, 102.

legal system.’<sup>55</sup> Thus comparative law provides ideas for solving a common problem by taking into consideration the social and economic circumstances.<sup>56</sup> This research investigates common issues that a regulator faces when overseeing financial services and stock markets in order to make suggestions for reform of the current financial law and best practices to adopt. It uses a comparative method to compare the Kuwaiti legal system and the UK legal system in terms of regulations of the financial sector. It also explores the risk-based framework in Kuwaiti capital markets to formulate financial regulations that are sufficient and appropriate.

The UK system was chosen as the basis for evaluating Kuwaiti law for several reasons. Firstly, Kuwait and the UK have a shared history because Kuwait was a British protectorate from 1899 to 1961.<sup>57</sup> The effects of Kuwait’s period as a British colony can be seen at many levels; for example, the first bank in Kuwait was established in 1941 by British investors. Second, both countries have specific and complete securities regulations that govern the markets. Third, both countries have a specialised entity for financial affairs – the CMA in Kuwait and the FCA in the UK. Fourth, the UK has up-to-date laws and regulations regarding financial markets, in addition to a comprehensive system for regulating the supervisory authority.

This research evaluates insider trading regulations in stock markets using risk-based approach as lends to analyses the data. It explores the regulation of financial services and stock markets in terms of supervision and enforcement procedures in the Kuwaiti legal system measured against IOSCO standards<sup>58</sup> and the UK’s approach to such regulation. It aims to use comparative approaches to reveal the deficiencies of the Kuwaiti financial system and suggest better regulations. Thus it adopts a critical comparative analysis method to study the two jurisdictions. There is a discussion of the methodology used in terms of data collection and analysis in Appendices 1 and 2 to this thesis.

## 5.1 Fieldwork

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<sup>55</sup> Kamba, 492; also see Jonathan Hill, ‘Comparative Law, Law Reform and Legal Theory’ (1989) 9 Oxford Journal of Legal Studies, 101, 106.

<sup>56</sup> Jonathan Hill, above, (n 55) 106.

<sup>57</sup> Faisal AbuSleb, ‘The fundamental phases of Kuwait foreign policy’ (Social Science Journal volume 43, no.4 2015, Kuwait University) 98 available at <<<http://drabusulaib.com/wp-content/uploads/2019/10/الرئيسية-المراحل-الخارجية-الكويت-سياسة-تطور-في.pdf>>> accessed 13 March 2020.

<sup>58</sup> IOSCO, ‘Objectives and Principles of Securities Regulation’, June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 6 February 2020.

The second stage of this research involved interviews with experts in the financial field. The interviews were semi-structured with open-ended questions to explore the experts' opinions about the CMA's policies regarding financial regulation in Kuwait. A list of the interview questions is attached to this thesis in Appendix 3. The purpose of these interviews was to understand public policy and validate the research findings.<sup>59</sup>

The seven interviewees were selected based on their practical experience in the financial sector and their positions in the CMA, whether in drafting the CML or in enforcing the law in courts, to gain insights about the law. It is important to clarify that none of the interviewees was identified while analysing the data collected for the thesis to ensure that their contributions remained anonymous. However, their individual positions as key actors in the financial system must be noted, to validate their contributions to the research. Their titles and descriptions of their positions are outlined in the following subsection to demonstrate that their contributions were very important for this research.

All the interviews were necessary to understand the unwritten rules and gain insights into financial regulations. It was important to include first-hand accounts of the CML to add personal knowledge about unwritten policies. The interviews were designed to give the interviewees the space and freedom to speak frankly about underlying policies and political arguments about the CML. There is no doubt that important laws like the CML were not created without compromise and agreement among all political parties in Kuwait. Understanding unwritten disputes about the CML and how its final formulation was developed helped to suggest solutions to the issue from a practical point of view.

#### 5.1.1 Data collection procedures and protocols

It is unusual to discuss practical and political issues with top experts in the financial legal system. Accordingly, from day one of the PhD journey the researcher worked closely with CMA staff and experts in the field to have the opportunity to ask for interviews. None of the interviews would have occurred without the researcher's efforts to attend events about the CMA and contacting the organisers to ask follow-up questions.

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<sup>59</sup> Aashish Srivastava and S Bruce Thomson, above, (n 43) 75. See also Robert Yin, above, (n 45 ) 110.

Firstly, it is necessary to explain the interview process from the initial stage of obtaining ethics approval. The researcher followed Warwick Law School protocol and obtained ethics approval from the competent authority at Warwick University.

Secondly, the researcher contacted each interviewee separately to schedule an interview. All the interviews were taken between 1 May 2019 and 9 June 2019. Each interview had its own challenges and obstacles. The first interview was with Participant No. 1, a former minister. The minister had a session at a Kuwait International Law School conference on 2 May 2019, so the researcher met him at the conference and asked for a meeting. He agreed to meet. Participant No. 1 is a former Minister of Commerce and Industry, the minister responsible for the CMA from 2015 to 2017. He was also a member of the committee that drafted the CML in 2010. The committee was responsible for reviewing the proposed law to arrive at the final version of the CML in 2010. He was appointed commissioner of the CMA from 2010 to 2012. He completed a PhD in international law from Paris-Sorbonne University in 1988 and is currently a professor and the dean of Kuwait International Law University. He provided insightful information about underlying policies and how the CML was developed to reach its final formulation.

The second interviewee was Participant No. 3, a former prosecutor and associate professor. The researcher met him in 2015 at a Kuwait University conference regarding the CML and its implementation. The researcher had previously discussed the latest amendments to the financial regulation in 2015 with the associate professor, so he was aware of her topic and her study. Participant No. 3 is an associate professor at Kuwait University who is an expert in criminal procedures and specialises in financial crime. He has published books and articles about the weaknesses of the Kuwaiti criminal system and its inability to prevent financial crime. He is currently a member of the CMA Complaint Committee, which is responsible for reviewing any complaint from listed companies about disclosure or insider dealing. He was able to comment on listed companies' complaints and the most challenging difficulties they face when dealing with financial regulations. He provided insightful information about how prosecutors investigate financial crime and how courts deal with such crime. He also commented on how the CMA deals with insider dealing and the internal procedures to investigate such crime. This helped validate the research findings about the weaknesses of enforcement procedures in the CMA.

The third interview was with Participant No. 2, a former commissioner of the CMA. The researcher contacted the interviewee through his law office in Kuwait City; she had previously discussed her research in conferences and at other events, so the interviewee knew about her topic and her intention to interview him. He is an associate professor who holds a PhD in public law and currently works as a private lawyer specialising in financial market litigation. He provided comments and feedback from a contrasting point of view as a former commissioner and private lawyer. He examined the law from a different perspective, which helped validate the lack of understanding of the CML in the field. His experience as a commissioner allowed him to provide insightful information about the policies underlying the 2015 amendments because he was a member of the amendment committee at that time.

The fourth interview was with Participant No. 7, the judge who works at Kuwait International Law School as an associate professor. The researcher went to a conference at the university on 2 May 2019 and asked for a meeting. After meeting at his office in the School of Law, the judge insisted that the researcher should meet the chairman of the CMA to raise questions and concerns. The researcher welcomed the idea but was concerned that she had no connection with the CMA chairman. The judge kindly contacted the chairman in person to arrange a meeting for the researcher. He is a judge from the appeals court who has a PhD in commercial law. He made comments about the application of financial regulations and the challenges that judges and prosecutors face when investigating financial crime. He gave insights about the most secretive sector in Kuwait – judges do not usually participate in social events or make comments about the judicial sector. His comments helped provide an understanding of weaknesses regarding investigating financial crime in the judicial sector, and of the reason why most insider dealing cases fail at the trial level.

The fifth interviewee was Participant No. 5, the current chairman of the CMA. The researcher met the chairman in his office at the CMA; he was aware of the researcher's work as she had presented a chapter of this thesis in Kuwait at a conference in 2018. He is a professor who holds a PhD in private law and has published several books and journal articles about insider dealing in Kuwait. His expertise in the field helped validate the research findings and allowed an understanding of the reasons why some solutions are not applicable in the context of Kuwait due to cultural differences and knowledge of financial regulations. This interview was the most

significant contribution to the research, as it provided unpublished information about the CMA's policies regarding regulating and supervising stock markets.

The sixth interview was with Participant No. 4, a junior assistant professor who had recently joined Kuwait University. The researcher had no connection with him but sent an email asking for a meeting to conduct an interview as part of the research, and he immediately agreed. He recently published a book about the CMA, including the most recent amendments in 2015. This is the only book to discuss and address the weaknesses of the 2015 amendments.

Finally, the seventh interviewee was Participant No. 6, an employee at the CMA Disclosure Department. The researcher sent an email asking for a meeting; the interviewee agreed, but insisted that the meeting be held outside the CMA due to the sensitivity of the topic. He provided comments and feedback about the internal procedures to deal with listed companies' disclosure. He previously worked at a listed investment company before joining the Disclosure Department. His experience helped highlight weaknesses in disclosure regulations. He made comments about how the Disclosure Department deals with inaccurate disclosures and the challenges that listed companies face in practice. These comments and the feedback helped provide a broader picture of the research findings and the CML's enforcement abilities.

All other meetings were conducted in the interviewee's office, at either a university or the CMA. These formal environments were helpful for obtaining the best answers to the questions. The interviewees were relaxed and spoke frankly about the current position of financial regulation in Kuwait. They addressed the challenges encountered in practice and welcomed any solution. All the interviews were conducted in Arabic, and lasted between 60 and 145 minutes. Most interviews were recorded, while notes were taken in other meetings. The researcher transcribed the interviews in Arabic and coded them based on the key issues and research findings for thematic analysis.

#### 5.1.2 Interview questions and rationale

The data collection process included semi-structured interviews with open-ended questions to explore experts' views and insights about the CML and its practical issues. For each interview the questions were constructed differently, with a focus on four categories: contextual,

diagnostic, evaluative and strategic aspects of Kuwait's CMA.<sup>60</sup> The questions were categorised using a thematic approach according to the key issues and framework of the thesis. The questions were not designed to have equal weight because each interviewee had experience in different areas of the field. For example, the former minister's questions related to political influence and the underlying policy of the CML, whereas the judge's questions focused on application of the law. These semi-structured interviews guide the conversation to focus on the research areas, but allow standardisation of the questions to make the data more reliable and to investigate the focus areas. The researcher did not share the questions with any interviewees in advance to ensure their answers were truthful, spontaneous, reliable and original. Additional questions were asked during the interviews as follow-ups to clarify or validate findings. It seems that semi-structured interviews with open-ended questions help obtain information about unwritten rules and policies. The data collected were strengthened by asking questions based on thematic codes and key issues to validate the research findings.

It is important to ensure that the researcher is not biased and does not ask leading questions. The open-ended questions (listed in Appendix 3) for the semi-structured interviews were designed and discussed with the researcher's supervisor to ensure they were well drafted. The researcher conducted macro-interviews with PhD students at Warwick University to improve the quality of the questions. Furthermore, the interviews required diplomatic skills to ask the right questions, accept the answers and then ask follow-up questions, but not to influence the interviewees. The researcher must be neutral and open-minded to accept any controversial answers. It is believed that this was successfully achieved.

## **6. Limitations to and significance of the research**

There is an extensive literature regarding financial regulation, but guidance on governance issues for public bodies remains unclear. Despite the substantial body of literature dealing with capital market governance and its many dimensions, most studies focus on Western countries. As all participants stated in their interviews, Kuwaiti law schools do not teach capital market regulation or securities law, thus very few studies have examined capital market regulation in Kuwait, either in general or in terms of international standards. Among these studies, only four have directly investigated regulation of the capital market and the work of the 'new' Kuwaiti

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<sup>60</sup> Ritchie and Spencer, above (n 40) 173, 178.



CMA in light of IOSCO standards for such regulation.<sup>61</sup> None of the studies has explored the risk-based approach used in Kuwait for financial regulation or the whistleblowing system in stock markets in the country.

The research topic was chosen because there seems to be a lack of effective insider trading supervision of financial services and the stock market in Kuwait. Prior research has shown that government influence is brought to bear over CMA decisions in relation to the market or particular institutions.<sup>62</sup> This needs to be addressed by adopting international standards and applying good governance regulations. The relative absence of effective supervision by the CMA has led to a lack of adequate protection for investors from insider trading. The main practical relevance of the research is that its results can provide regulators, legislators, judges and prosecutors with a clear understanding of the concept of effective supervision and enforcement, particularly related to insider dealing. It is important to have a common set of standards and behaviour that can attract investors. A risk-based approach and the application of IOSCO standards can create an appropriate legal framework for investors. The CMA needs to enhance the level of awareness and appreciation of good regulation to increase trust and build confidence in the Kuwait stock market.

## 6.1 Previous studies

There is a lack of studies on the Kuwait CMA. Most are outdated, and do not make effective contributions to the field because they are either too descriptive or repetitions of older studies. In terms of existing studies, a 2009 paper by Dr Amani K. Bouresli regarding the application of IOSCO Principles in Kuwait was published before the latest CML amendment in November 2015.<sup>63</sup> A book by Dr Bader AlMullah on the legal structure of the capital market was published in 2012, also before the 2015 amendment.<sup>64</sup> A book by Dr Hussain Boaruki on legal protection of the CMA was published in 2016,<sup>65</sup> as was a paper by Dr Asim Jusic and Dr Farah Yassen

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<sup>61</sup> Amani K. Bouresli, 'A Study of the Regulatory & Organizational Structure of the Capital Market of Kuwait in the Light of the IOSCO Principles & the World Bank Report' (2009) 35 *Journal of the Gulf and Arabian Peninsula Studies*. Fatima Al Shurian, above (n 4). Abdullah Alshebli, 'The Protecting Individual Investors under Kuwaiti Securities', above, (n 4). Asim Jusic, Farah Yassen, above, (n 30).

<sup>62</sup> Bader Al-Mullah, *Legal Structure for Capital Market* (2nd edn, 2012) 300; see also Asim Jusic and Farah Yassen, above (n 30) 33

<sup>63</sup> Amani K. Bouresli, above (n 61).

<sup>64</sup> Bader AlMullah, above (n 62)

<sup>65</sup> Hussain Boaruki, *The Legal Protection for Capital Market Authority: Case Study of Kuwait and France*, above, (n 4)

concerning international standards and the administrative model of capital market regulation in Kuwait.<sup>66</sup> A study by Abdullah AlKharafi and Abdullah AlHaroun regarding Kuwait's securities law was also published in 2016.<sup>67</sup> Finally, a book by Dr Abdullallah AlHayyan and Mohamad Almutairi explaining the CML and its amendments was published in 2019.<sup>68</sup>

Some academic theses have also investigated Kuwait's securities law, but the majority of these were published before the latest CML amendments and its Executive Bylaw No. 72 of 2015. The amended law became effective in November 2015 and the amendments were significant,<sup>69</sup> covering most aspects of the CML. The relevant theses are Fahad AlZumai, 'Protection of Investors in Gulf Cooperation Council Stock Markets: A Case Study of Kuwait, Bahrain, and United Arab Emirates', published in 2006;<sup>70</sup> Fatima AlShuraian, 'Market Manipulation in Kuwait Stock Exchange', published in 2013;<sup>71</sup> Abdullah R. A. S. Alshebli, 'Protecting Individual Investors Under Kuwaiti Securities Law', published in 2015;<sup>72</sup> Samar Salah Abdullallah's 2015 thesis on using insider information in stock markets according to Law No. 7 of 2010 and the 2015 amendments;<sup>73</sup> and Dr Mohamad Almutairi, 'A Critical Assessment of Regulation of Insider Trading Under the Kuwait CMA Law', published in 2018.<sup>74</sup> To the best of the researcher's knowledge, these are the only studies that have evaluated Kuwait's CML; thus the present study is the first to investigate Kuwait's CMA in relation to the application of a risk-based approach and a whistleblowing system for the regulation and application of international standards for supervision and enforcement.

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<sup>66</sup> Asim Jusic, Farah Yassen, above, (n 30). 44.

<sup>67</sup> Abdullah AlKharafi and Abdullah AlHaroun above, (n 38) 187

<sup>68</sup> Abdullallah AlHayyan and Moahamad AlMutairi, *AlWaseet For Explanation of Kuwait Financial Law*. (Dar AlAlam 2019)

<sup>69</sup> Hussain Boaruki, 'Ten Important Points About the New Amendment of the Capital Markets Law' *AlQabas* (Kuwait, 23 April 2018) <<https://www.alanba.com.kw/ar/economy-news/553297/23-04-2015---نقاط-قوة-في-تعديلات>> accessed 18 March 2020.

<sup>70</sup> Fahad Al-Zumai, 'Protection of Investors in Gulf Cooperation Council Stock Markets: A Case Study of Kuwait, Bahrain and United Arab Emirates' (PhD, School of Oriental and African Studies (University of London) 2006). This thesis was completed before the issuance of the Capital Market Law in 2010 and even prior to the financial crisis of 2007–2008.

<sup>71</sup> Fatima AlShuraian, above, (n 4**Error! Bookmark not defined.**).

<sup>72</sup> Abdullah Alshebli, 'The Protecting Individual Investors under Kuwaiti Securities', above, (n 4**Error! Bookmark not defined.**) The author submitted his thesis before the amendments were issued in May 2015.

<sup>73</sup> Samar Abdullallah, 'Preventing using Inside Information in Stock Markets According to Law No.7 of 2010 regarding the establishment of Capital Markets Authority' (Master Dissertation, Kuwait University 2015). This thesis was completed before the latest amendments, which were issued in May 2015. The only available copy is in the library at Kuwait University as a hard copy.

<sup>74</sup> Mohammad Al-Mutairi, above, (n 24**Error! Bookmark not defined.**).

## **7. Thesis structure**

The thesis consists of nine chapters.

Chapter 1: This chapter introduces the study and covers the main components of the research proposal, such as context, objectives, significance and methodology.

Chapter 2: This chapter outlines the regulator's policy in using financial regulation and the key principles involved in applying a risk-based approach, highlighting the importance of adopting a clear policy in designing financial regulation. It defines and provides a rationale and application of risk-based and forward-judgement-based regulation in Kuwait's context. Thus it addresses the challenges that the regulators and financial institutions are likely to experience in applying a forward-looking judgement-based approach. It also aims at investigating the appropriate conditions and requirements for the formulation of a judgement-based approach in Kuwait.

Chapter 3: The chapter gives a brief background of Kuwait's oversight system and the legal framework governing the CMA in terms of its relationship with other supervisory authorities. It discusses the regulatory framework for stock markets and private institutions' role in promoting strong securities markets.

Chapter 4: This chapter addresses issues of accountability, independence, funding, coordination, cooperation and the importance of the CMA in protecting the public interest. It seeks to evaluate the current legal framework of the CMA in Kuwait by referring to the UK approach, and to suggest better regulation of the CMA's independence and accountability.

Chapter 5: The chapter examines the legal framework for the enforcement and invocation of the CMA's supervisory powers. It explains the compliance and deterrence-based approaches in relation to the CMA's enforcement mechanism. It assesses the CMA's investigative power and proposes best practices taken from the UK. It also explains the advantages and disadvantages of civil and criminal penalties used by the CMA. Essentially, this chapter discusses the CMA and CML enforcement mechanisms *vis-à-vis* the UK's FCA. In addition to the application of IOSCO standards, it evaluates the Kuwaiti approach by drawing inspiration from the UK in enforcing capital market rules and regulations. The chapter evaluates the capability of the CMA to protect the markets in terms of its human capital and regulatory tools.

Chapter 6: This chapter investigates the disclosure regime in the Kuwaiti system. It aims to explain the importance of information disclosure on time in preventing insider trading. The disclosure regime is one of the precautionary measures to prevent market abuse by enforcing disclosure of fundamental information by regulated firms and individuals. The chapter evaluates the disclosure regulations to reveal the weaknesses in disclosure obligations.

Chapter 7: This chapter explains the CMA's policy on preventing insider dealing. It provides a definition of insider trading in the Kuwaiti system, and evaluates regulatory clarity and effectiveness in terms of preventing insider dealing.

Chapter 8: This chapter exposes Kuwait's policy on a whistleblowing system. It identifies the legal channel to whistleblowing in stock markets, analyses whistleblowing regulation by referring to the UK approach to reveal the deficiencies in the Kuwait system and evaluates regulation clarity and effectiveness in terms of capturing insider dealing.

Chapter 9: This chapter summarises the research findings and provides key recommendations to the government and the CMA.

## Chapter 2: The Risk-Based Approach

### 1. Introduction

Before the financial crisis in 2008 the UK regulators followed a risk-based approach to regulation. This helped to develop and improve financial regulations, but did not prevent the financial crisis. Consequently, after the 2008 crisis the UK adopted a new style of regulations, the forward-looking judgement-based approach. The risk-based approach was ineffective in the UK mainly because of insufficient application of the approach by the former financial regulator (the FSA).<sup>75</sup> The crisis highlighted deficiencies in the approach, such as insufficient communication between the supervisory authority and firms.<sup>76</sup> However, there is still a belief that a risk-based approach is a good strategy in regulating the financial industry.<sup>77</sup>

In Kuwait the best approach to regulating financial services and stock markets has not been specified or published, but one interviewee (Participant No. 1) clarified that there has been a movement in the Kuwait CMA to shift from a deterrence-based approach towards a risk-based approach. For example, the recent instruction from the CMA regarding ‘adequacy capital’<sup>78</sup> highlighted the CMA’s efforts to adopt such an approach to financial regulation.

Academic commentators might ask why Kuwait wants to adopt risk-based approach to regulation after it failed to help the UK regulator in preventing the 2008 financial crisis. First, the risk-based approach did not fail to prevent the Northern Rock crisis; rather, the UK

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<sup>75</sup> The Financial Service Authority ‘The supervision of Northern Rock: a lessons learned review’ (2008) [Online] Available: <<https://www.fca.org.uk/publication/corporate/fsa-nr-report.pdf>> accessed 13 March 2020. See also Financial Conduct Authority ‘The FCA’s approach to advancing its objectives’ (2015) Available: <<https://www.fca.org.uk/publication/corporate/fca-approach-advancing-objectives-2015.pdf>> accessed 13 March 2020.

<sup>76</sup> David Bholat, James Brookes, Chris Cai, Katy Grundy and Jakoob Lund, ‘Sending firm message: text mining letters from PRA supervision to banks and building societies they regulate’ (2017) Bank of England Working Paper No.688, 1 << <https://www.bankofengland.co.uk/working-paper/2017/sending-firm-messages-text-mining-letters-from-pra-supervisors-to-banks-building-societies>>> accessed 13 March 2020

<sup>77</sup> Financial Conduct Authority ‘The FCA’s approach to advancing its objectives’ (2015) Available: << <https://www.fca.org.uk/publication/corporate/fca-approach-advancing-objectives-2015.pdf>>> accessed 13 March 2020. See also IOSCO, ‘Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries’, (2009) 3 available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>> accessed 13 March 2020.

<sup>78</sup> The CMA website available at <<https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/detail/646747>> accessed 18 March 2020. Participant no.1 confirms there is policy towards adopting risk-based approach

financial regulator at that time failed to apply the approach correctly.<sup>79</sup> It seems that the UK financial regulator gave low priority to prudential supervision, which led it to allocate insufficient resources to high-impact banks like Northern Rock.<sup>80</sup> In fact, the UK regulatory reform committee stated that: ‘In evidence, there was general agreement that risk-based regulation was not of itself a cause of the financial crisis, although the application of a risk-based approach had been faulty.’<sup>81</sup>

There are good examples of the application of the risk-based approach in jurisdictions like Australia and Canada.<sup>82</sup> In other words, the efficacy of risk-based regulation depends on how it designed and implemented. It is important to design the risk-based approach taking into consideration how it operates in practice and the compliance culture in the market. Kuwait must learn from the UK mistakes in creating and implementing its own risk-based approach to regulations.

Finally, the discussion about risk-based regulations in Kuwait is very limited, so this thesis proposes what such regulations should look like. It is important to highlight that if the risk-based approach to regulation is itself regulated poorly, it will devastate the industry. This thesis explains what a risk-based approach to regulation should look like in a Kuwaiti financial services context.

The fieldwork revealed a lack of knowledge of the risk-based philosophy and how it works. Apart from Participant No. 1, the interviewees stated that they do not understand the risk-based approach. Based on the fieldwork, this chapter includes a section about risk in context to explain the concept of the approach. It starts with a background section covering the events that led to the new approaches, either risk-based or judgement-led, and then analyses the two approaches to decide the best fit with CMA policy on supervising and enforcing regulations in the financial sector. The questions here are whether the risk-based approach to regulation is sufficient, or would a judgement-led approach be better. There are various factors to

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<sup>79</sup> The Financial Service Authority ‘The supervision of Northern Rock: a lessons learned review’ (2008) [Online] Available: <<https://www.fca.org.uk/publication/corporate/fsa-nr-report.pdf>>accessed 13 March 2020.

<sup>80</sup> Julia Black, ‘*The Regulatory Styles and Supervisory Strategies*’ (2015) The Oxford handbook of financial regulation 231.

<sup>81</sup> Financial Conduct Authority ‘The FCA’s approach to advancing its objectives’ (2015) [Online] Available: <<<https://www.fca.org.uk/publication/corporate/fca-approach-advancing-objectives-2015.pdf>>> accessed 13 March 2020.

<sup>82</sup> Julia Black, ‘*The Regulatory Styles and Supervisory Strategies*’ above (n 80) 243. OECD Review of Regulatory Reform, ‘Regulatory Impact Analysis: A Tool for Policy Coherence’ (2009).

consider in adopting a strategy on regulation, namely the culture and the political and institutional context. This chapter explains risk-based regulation and highlights its role, including advantages and disadvantages of the approach. It concludes by assessing the two approaches and introducing the structure of this thesis.

## **2. Background**

The collapse of the second oldest merchant bank in the UK, Barings, in 1995 had a major impact on the philosophy of the UK oversight of financial markets. This was the trigger for the UK regulator to adopt a risk-based approach. The collapse raised questions about risk management controls and their oversight of trading operations and ability to protect the markets. The main reason for the collapsing of Barings Bank was the significant losses in one of its subsidiary companies, Barings Futures Singapore (BFS).<sup>83</sup> The losses were the result of unauthorised trading in the futures market by Nicholas Leeson, a BFS executive who was authorised to trade only between the Singaporean and Osaka Futures Exchanges as part of a switching operation.<sup>84</sup> Leeson engaged in highly risky financial contracts, known as options, without Barings' knowledge, which led to the collapse.<sup>85</sup> The Bank of England (BoE) announced at the end of December 1994 that there were cumulative unrecognised losses in Barings' accounts of over £385 million. By 27 February 1995 the reported losses reached £950 million.<sup>86</sup>

Although a report by the Board of Banking Supervision cleared the BoE of responsibility for the collapse of Barings Bank, there was clearly a need for greater regulation in the UK supervisory strategy. Firstly, there needed to be improved understanding of the risks of non-bank business. For example, it was unclear who was responsible for the supervision of Nicholas Leeson's activities.<sup>87</sup> Secondly, there was a need to develop communication between the international supervisory authorities. The domestic responsibilities of the

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<sup>83</sup> Andrew Brown, 'Making sense of the collapse of Barings Bank' (2005) 58 Human Relations 1579, 13 available << <https://journals.sagepub.com/doi/10.1177/0018726705061433>>> accessed 13 March 2020.

<sup>84</sup> Reserve bank of Australia Bulletin 'Implication of the Barings Collapse for Bank supervisors', (November 1995) available at <<https://www.rba.gov.au/publications/bulletin/1995/nov/pdf/bu-1195-1.pdf>> accessed 13 March 2020 See also Alison Lui, 'Regulation and Corporate Governance : A Case Study of the UK Banking Industry' (PhD thesis, university of Liverpool 2014) 31.

<sup>85</sup> Andrew Brown, 'Making sense of the collapse of Barings Bank' (2005) 58 Human Relations 1579, 13.

<sup>86</sup> Reserve bank of Australia Bulletin 'Implication of the Barings Collapse for Bank supervisors', (November 1995) available at <<https://www.rba.gov.au/publications/bulletin/1995/nov/pdf/bu-1195-1.pdf>> accessed 13 March 2020. 2

<sup>87</sup> Ibid., 3.

regulatory authorities were not clear, and the lack of coordination among the authorities weakened the supervisory system.<sup>88</sup> Thirdly, it was vital to obtain information from banks' internal audits.<sup>89</sup> Fourthly, the oversight system relied on people, controls, capital and liquidity, and there were clearly problems with the 'people' element.<sup>90</sup> The people were inexperienced, and did not provide adequate support to uncover illegal activities. Furthermore, there was a lack of management controls in the bank which enabled Leeson to engage in unrecognised transactions without Barings' knowledge.<sup>91</sup> The most important factor is that the risks were not well understood.<sup>92</sup> Finally, it was necessary to understand the relationship between financial regulation and financial crime legislation to develop a more effective supervision strategy.<sup>93</sup>

In this context, the collapse revealed the weakness of multiple regulators in supervising the banking sector, and this led to the adoption of a single financial regulator model. There was an important reform of UK financial regulation in 1997 when the FSA<sup>94</sup> was established.<sup>95</sup> Statutory powers were given to the FSA by the FSMA 2000 (FSMA). The FSA<sup>96</sup> was responsible for the supervision of all financial markets, insurance and retail financial services in the UK.<sup>97</sup> The supervisory responsibilities had previously been split between multiple regulators, but this arrangement ended with the establishment of the FSA.

In fact, the roots of the risk-based approach can be traced back to the BoE in developing the supervisory strategy.<sup>98</sup> The BoE was already in the process of developing a system to

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<sup>88</sup> Joseph Norton, 'Global Financial Sector Reform: The Single Financial Regulator Model Based on the United Kingdom FSA Experience-A Critical Reevaluation' (2005) 39 *International Lawyer*, 15,23.

<sup>89</sup> Reserve bank of Australia Bulletin 'Implication of the Barings Collapse for Bank supervisors', (November 1995) available at <<https://www.rba.gov.au/publications/bulletin/1995/nov/pdf/bu-1195-1.pdf>> accessed 18 March 2020.

<sup>90</sup> Laura Proctor, 'The Barings Collapse: A Regulatory Failure, or a Failure of Supervision' (1997) 22 *Brooklyn Journal of International Law* 735, 751.

<sup>91</sup> *Ibid.*, 752

<sup>92</sup> Andrew Brown, above, (n 83) 19-20

<sup>93</sup> Nicholas Ryder, 'The financial crisis and financial crime in the United Kingdom: A critical analysis of the response by Financial Regulatory Agencies' (2017) 38 *The Company Lawyer*, 4, 5-7.

<sup>94</sup> It created immediately after the May 1997 general election by the new Labour Government.

<sup>95</sup> Joseph Norton, above, (n 88) 23, See also Duncan Alford, 'Core Principles for Effective Banking Supervision: an Enforceable International Financial Standard' (2005) 28 *Boston College International and Comparative Law Review* 237, 273-273.

<sup>96</sup> Now, The FSA has become two separate regulatory authority namely: The Financial Conduct Authority which is responsible for conduct of business, and The Prudential Regulation Authority which is part of the Bank of England and responsible for prudential regulation.

<sup>97</sup> Adam Tickell, 'Success and Failure in the UK sector the Baring Crisis', (1999) Paper Presented at the ECPR Joint Sessions, Workshop 16 Success and Failure in Governance

<sup>98</sup> Julia Black, '*The Regulatory Styles and Supervisory Strategies*' above, (n 80) 245



evaluate and assess risk when the UK regulator adopted a risk-based approach after the Barings collapse.<sup>99</sup> The system created was termed 'risk assessment, tools and evaluation' (RATE). The FSA realised that a post-event rule-based strategy can be an effective way to supervise and enforce financial regulation or avoid financial crisis.<sup>100</sup>

RATE was the first step towards a risk-based approach to regulation, but the FSA enhanced the system to create the 'advanced regulatory risk operating framework' (ARROW). This was developed by small group formed in 2001 to design a risk-based system.<sup>101</sup> The stated aim of ARROW was 'to provide a common risk assessment framework for all firms regulated by the FSA, and to promote a regulatory approach that is proactive, integrated and transparent'.<sup>102</sup>

Briefly, ARROW is a framework to determine regulatory priorities and resource allocation.<sup>103</sup> It is a strategy to lead the regulator to focus its resources on certain risks which might affect its statutory objectives. There are seven risks to objectives: financial failure, misconduct or mismanagement, consumer understanding, fraud or dishonesty, market abuse, money laundering and market quality. ARROW is a useful system to protect the markets from these risks. It is important to clarify that the FSA focused its resources on risks that might prevent it from achieving its statutory objectives.<sup>104</sup> The risk-based approach to regulation reshaped the relationship between the regulator and licensed persons: some risks will be handled by the licensed person only, while others will be shared responsibilities. For example, the

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<sup>99</sup> Julia Black, 'The Emergence of Risk-Based Regulation and the New Public Risk Management in the United Kingdom' (2005) Public law, 510, 512.

<sup>100</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) 8 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 13 March 2020.

<sup>101</sup> Julia Black, 'The emergence of risk-based regulation and the new public risk management in the United Kingdom' above, (n 99) 526.

<sup>102</sup> Julia Black, 'The emergence of risk-based regulation and the new public risk management in the United Kingdom' above (n 99) 527 See also International Monetary Fund, 'United Kingdom : IOSCO Objectives and Principles of Securities Regulation: Detailed Assessment of Implementation' (3 August 2011) available <<<https://www.imf.org/en/Publications/CR/Issues/2016/12/31/United-Kingdom-IOSCO-Objectives-and-Principles-of-Securities-Regulation-Detailed-Assessment-25124>>> accessed 18 March 2020.

<sup>103</sup> Julia Black, 'The emergence of risk-based regulation and the new public risk management in the United Kingdom' above, (n 99) 529.

<sup>104</sup> Julia Black, 'The Development of Risk-Based Regulation in Financial Services: `Just `Modelling Through`?', 156 in Black Julia, Lodge Martin and Thatcher Marck, *Regulatory Innovation a Comparative Analysis* (Edward Elgar Publishing, 2005). See also International Monetary Fund, 'United Kingdom : IOSCO Objectives and Principles of Securities Regulation: Detailed Assessment of Implementation' (3 August 2011) available <<<https://www.imf.org/en/Publications/CR/Issues/2016/12/31/United-Kingdom-IOSCO-Objectives-and-Principles-of-Securities-Regulation-Detailed-Assessment-25124>>> accessed 18 March 2020.

responsibility of the senior management of a company will be clearly and precisely to control certain risks based on a risk assessment against the company's goals.

The risk-based approach to regulation adopted in the UK replaced the rule-based approach used by former regulators. Rule-based regulations were insufficient to protect the financial markets from bank collapse, and it was such collapses that prompted change in the UK strategy in supervising the financial sector. The regulations were inflexible and unable to capture or understand new risk in the markets. In 2005 the Hampton Report encouraged all the regulatory agencies to adopt a risk-based approach for better regulation.<sup>105</sup> This recommendation changed the strategy of most of the regulators, and moved the UK from responsive regulation to a risk-based approach to supervising licensed persons. The risk-based approach was tested by the 2008 financial crisis: the Northern Rock bank collapse proved that risk-based regulation had only a limited ability to protect the financial markets, just like principle-based regulation.<sup>106</sup> The FSA failed to protect its statutory objectives because of light-touch regulation.<sup>107</sup> Risk-based regulation can assess the current risks that affect the statutory objectives, but cannot investigate or calculate the overall business strategy or future risks.<sup>108</sup> The concept of risk-based regulation is to control excessive risks that affect the statutory objectives.<sup>109</sup> The FSA's policy focus is on the assessment of a firm's risk against its statutory objectives using the ARROW operating framework.<sup>110</sup> So risk-based regulation calculates only risks that may harm or affect the obvious statutory objectives, but many 'uncertainty' risks do not have a direct effect on the statutory objectives. The ARROW system does not recognise unfamiliar risk and focuses only on measurable risk, hence risk-based regulation cannot calculate uncertainty risks.<sup>111</sup> The Northern Rock bank failed to achieve the FSA's objectives in terms of its ability to fund its operation without the need for

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<sup>105</sup> Philip Hampton, 'Reducing Administrative Burdens: Effective Inspection and Enforcement: Final Report' (March 2005) HM Treasury, London.

<sup>106</sup> Joanna Gray, 'Is it time to highlight the limits of risk-based financial regulation' (2009) 4 Capital Markets Law Journal, 50, 51.

<sup>107</sup> It is important to clarify that the FSA never use term 'light-touch' to describe its policy or regulation. see Iain MacNeil, *An Introduction to the Law on Financial Investment*, (Oxford and Portland, Oregon, 2012) 105. see FSA, 'The Turner Review, A Regulatory Response to the Global Banking Crisis' (March 2009) available at <<[http://www.actuaries.org/CTTEES\\_TFRISKCRISIS/Documents/turner\\_review.pdf](http://www.actuaries.org/CTTEES_TFRISKCRISIS/Documents/turner_review.pdf)>> 13 March 2020.

<sup>108</sup> Iain MacNeil, above, (n 107) 104 -105.

<sup>109</sup> Iain MacNeil, 'Risk Control Strategies: An Assessment in the Context of the Credit Crisis' in Iain MacNeil and Justin O'Brien, *The Future of Financial Regulation* (HART Publishing Ltd, 2010) 143.

<sup>110</sup> Joanna Gray, above, (n 106) 53.

<sup>111</sup> Iain MacNeil, 'Risk Control Strategies, above, (n 107) 142.

liquidity assistance.<sup>112</sup> Both risk-based and principle-based regulation failed to capture risks at early stages, thus the supervisory strategy was insufficient to protect the markets.

Many studies of the UK-specific aftermath of the financial crisis centred on the 2008 Northern Rock bank collapse and its subsequent government nationalisation (or ‘bail out’).<sup>113</sup> Northern Rock exemplifies two further and interrelated concepts that have attracted significant scholarly and UK regulatory policymakers’ attention over the past ten years: ‘moral hazard’ and ‘too big to fail’ (TBTF).<sup>114</sup>

Moral hazard is the attitude encouraged in financial markets that no matter what risks the large institutions may assume in their pursuit of bigger rewards (profits), governments will ultimately never allow the institutions to fail.<sup>115</sup> In other words, the market participants (both institutions and the individuals making investment decisions within each institution) are encouraged to believe that no matter what may transpire in terms of investment losses, their actions will be excused by governments and their regulators. This attitude is an incentive to assume unreasonable risks.<sup>116</sup>

TBTF is the companion institutional and government policy attitude that, unlike other private enterprises where insolvency means a business will fail and cease to exist, the government will rescue a financial institution in the (perceived) national interest.<sup>117</sup> It is clear that the following points are well supported by this brief crisis summary. The inability of markets to provide effective self-regulation under a risk-based approach, combined with market regulators failing to identify and provide effective oversight regarding the dangers to the entire financial system posed by moral hazard and TBTF thinking, created the dynamic in which the crisis accelerated. The fact that the former financial regulator, the FSA (currently

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<sup>112</sup> Joanna Gray, above, (n 106) 54.

<sup>113</sup> *SRM Global Master Fund LP & Ors v HM Treasury* [2009] EWCA Civ 788 (CA (Civ)), as discussed by Hájek See Otakar Hájek ‘What Is Moral Hazard and How Was It Invoked in the UK During the Northern Rock Crisis in 2007?’ (2010) *Common Law Review*, 27-30; see also Bank for International Settlements (BIS) (2016). The syndicated loan market. [Online] Available: [http://www.bis.org/publ/qtrpdf/r\\_qt0412g.pdf](http://www.bis.org/publ/qtrpdf/r_qt0412g.pdf)> 30 December 2019

<sup>114</sup> David Strachan and Scott Martin ‘Quick action required to tackle too-big-to-fail banks’ (2016) 14(8) *G.R.R.* 23, 24-27. Available at << <https://www2.deloitte.com/uk/en/pages/financial-services/articles/tackling-too-big-to-fail.html>>> accessed 13 March 2020.

<sup>115</sup> Jacopo Carmassi and Elisabetha Luchetti and Stefano Micossi, Overcoming too-big-to-fail: A regulatory framework to limit moral hazard and free riding in the financial sector, 2010[Online] Available: <https://ssrn.com/abstract=1610214>> accessed 13 March 2020, 21, 22.

<sup>116</sup> Ibid.

<sup>117</sup> Ibid, see also Otakar Hajek, above, (n 113) 30.

the FCA), moved away from risk-based regulation to a new regulatory approach is not surprising when this decision is placed against this crisis background.

While endorsing a risk-based regulatory approach, the UK was placing its faith in the view that the markets will function more effectively when participants are not subject to ‘excessive’ regulation or face additional costs associated with regulatory compliance.<sup>118</sup> Risk-based supervision has its advantages, but improvements are still needed. It does not provide a risk assessment framework that is suitable for assessing the risks in diversified financial conglomerate groups.<sup>119</sup> The ability to identify the risks that markets are facing is problematic. With their pre-2007 mindset, policymakers believed that UK markets were more likely to attract business and the UK would be regarded as encouraging a strongly pro-business environment.<sup>120</sup> The 2008 crisis proved them wrong: the system has flaws, which led the regulator to adopt a new approach to supervising and enforcing regulation.

The following sections explain the risk-based approach and how the CMA can adopt it properly. It also clarifies the judgement-led approach and its application by the FCA.

### **3. Risk in context**

The adoption of risk as the basis of regulations is the core of a regulatory process where regulation must be proportionate to the risks.<sup>121</sup> It is a strategic organising principle to construct the regulatory management policy and allocate resources in the financial sector based on risk assessment to meet public expectations.<sup>122</sup> Defining risk is important to understand the philosophy of this policy: it involves the ability to assess an event associated with risk by mathematical calculation in order to predict and control the risk.<sup>123</sup> The existence of risk is one of the primary reasons to develop and improve rules and regulations, to protect

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<sup>118</sup> Paul Gopal, ‘A Critical Examination of the Impact of Section 172 of the Companies Act 2006’ (2016) [online] <<http://www.sjol.co.uk/issue-4/a-critical-examination-of-the-impact-of-section-172-of-the-companies-act-2006>> accessed 13 March 2020.

<sup>119</sup> Joseph Norton, above, (n 88) 32-33

<sup>120</sup> Financial Reporting Council (FRC), *Corporate Governance Code 2012*, [Online] Available: <<https://www.frc.org.uk/Our-Work/Codes-Standards/Corporate-governance/UK-Corporate-Governance-Code.aspx>> accessed 13 March 2020.

<sup>121</sup> Joanna Gray and Hamilton Jenny, *Implementing Financial Regulation: Theory and Practice* (John Wiley & Sons, 2006), 3.

<sup>122</sup> Michael Power, *The Risk Management of Everything: Rethinking the Politics of Uncertainty* (Demos 2004) 21, 37.

<sup>123</sup> Joanna Gray and Jenny Hamilton, above (n 121) 20.

human beings and the environment from resulting hazards or damage.<sup>124</sup> These rules oblige people to adopt certain procedures to control or mitigate risk. For example, a lack of water is a risk that people avoid by living in civilised societies to ensure the accessibility of water.

There are two theoretical perspectives that address risks as a basis for regulation: 'risk society' and 'governmentality'. The risk society theory is presented in the work of sociologist Ulrich Beck,<sup>125</sup> while the governmentality theory is found in the work of the French social thinker Foucault.<sup>126</sup>

Many risks occur in modern life. According to Beck, today we live in a 'risk society', and the risks we face at present are significantly different from those of previous historical eras.<sup>127</sup> They result from human activities in the process of industrial, modernising and capitalist development.<sup>128</sup> These risks led policymakers to make decisions based on risk assessments to provide more suitable regulations to achieve people's expectations. Risk-based regulation can be defined as 'the regulator's attempts to control risk by setting and enforcing products or behavioural standards'.<sup>129</sup>

In the financial industry the regulator avoids risk by setting rules to control and mitigate risks. Risks became the centre of the strategy to regulate the financial sector. As Fisher highlighted:<sup>130</sup>

One of the central tasks of the UK executive state is now perceived to be the handling of risk... The task of public decision makers is increasingly characterised in terms of the identification and assessment and management of risk and the legitimacy of public decision-making is also being evaluated on such a basis.

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<sup>124</sup> Christopher Hood, Henry Rothstein and Robert Baldwin, *The Government of Risk: Understanding Risk regulation regimes*, (Oxford University Press, 2001) 3, 4. See also Ulrich Beck, *World and Risk Society and Manufactured Uncertainties*, vol. 1, no. 2 (Firenze University Press, 2009) 292.

<sup>125</sup> Ulrich Beck, *Risk Society: Towards a New Modernity* (London and New York, SAGE, 1992) 11, 22-33. See Ulrich Beck, and Anthony Giddens: *Risk Society* 1992. See Ulrich Beck, *World and Risk Society and Manufactured Uncertainties*, above, (n 124), 298. See Joanna Gray and Jenny Hamilton, above (n 121) 22.

<sup>126</sup> Graham Burchell, Colin Gordon and Peter Miller, *The Foucault Effect: Studies in Governmentality* (University of Chicago Press, 1991) 88, See Michel Foucault, *The Foucault effect: Studies in governmentality* (University of Chicago Press 1991). Joanna Gray and Jenny Hamilton, above (n 121) 22.

<sup>127</sup> Ulrich Beck, *Risk Society: Towards a New Modernity*, above, (n 125) 22

<sup>128</sup> Ulrich Beck, *Risk Society: Towards a New Modernity*, above, (n 125) 297. See Ulrich Beck, *Risk Society* (1986) cited in Joanna Gray, and Hamilton Jenny. *Implementing Financial Regulation-Theory and Practice*. (2006) 7

<sup>129</sup> Christopher Hood, Henry Rothstein and Robert Baldwin, above, (n 124) 3

<sup>130</sup> Elizabeth Fisher, 'The Rise of the Risk Commonwealth and the Challenge for Administrative law' (2003) *Public Law*, 455 cited in Joanna Gray and Jenny Hamilton, above, (n 121) 2.

There are several risks in the financial sector, but the ones that must be targeted are those that affect the ability of the regulator to achieve its objectives.<sup>131</sup> It is important to stress that each jurisdiction has its own risk framework: what one regulator finds a low risk to its objectives, another regulator perceives as high risk.<sup>132</sup> Folarin Akinbami divided strategies of risk regulation into four types of risk.<sup>133</sup> First are the risks that people's behaviour poses to the community, such as those overseen by the Health and Safety Executive.<sup>134</sup> Second are the risks related to internal risk management systems, which means how firms deal with risks internally. Third are the risks related to the regulator's objectives and ensuring that the objectives are met.<sup>135</sup> These risks are mostly attached to the regulator itself and how it achieves its objectives, for example by using information technology systems, human planning resources or a disclosure regime. The regulator must ensure that the risks in these areas are mitigated.<sup>136</sup> Fourth are the risks related to the management of regulatory or institutional risks, which means the risk depends on how a licensed person behaves in trying to achieve the regulator's objectives.<sup>137</sup>

In contrast, the governmentality theory is focused on the identification of risk associated with individuals and institutional activities and behaviour to provide a tool to manage and control populations, groups or individuals in neoliberal societies.<sup>138</sup> It is centred on the idea of how risk can be used as tool of governance to correct behaviours. For example, when a government imposes an extra tax on smoking products because of the risk to environment and

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<sup>131</sup> International Monetary Fund, 'Kuwait: Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism (Report No. 11/268, September 2011) available << <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Detailed-Assessment-Report-on-Anti-Money-Laundering-and-Combating-the-Financing-of-25210>>> accessed 13 March 2020. See IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>> > accessed 13 March 2020.

<sup>132</sup> Julia Black and Robin Baldwin, 'When risk-based regulation aims low: Approaches and challenges' (2012) 6 *Regulation & Governance* 2-4.

<sup>133</sup> Folarin Akinbami, 'Improving Regulation Under the Financial Service and Markets Act 2000: The need for a more Assertive Approach to supervision and Implementation of Regulatory objectives (PhD thesis, University of Manchester, 2009) 189-190.

<sup>134</sup> Christopher Hood Henry Rothstein and Robert Baldwin, above, (n 124) 36-44.

<sup>135</sup> OECD, 'OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators' (2014) available << <https://www.oecd.org/gov/regulatory-policy/the-governance-of-regulators-9789264209015-en.htm>>> accessed 18 March 2020.

<sup>136</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>> > accessed 13 March 2020.

<sup>137</sup> *ibid.*

<sup>138</sup> Joanna Gray and Jenny Hamilton, above, (n 121) 9.

health, it encourages self-regulation by smokers to quit smoking to avoid paying the extra tax. This method governs individual and group behaviour by imposing certain type of regulations based on risk calculation, without state intervention to redefine individuals' responsibility to manage their own risks in society voluntarily.

This section demonstrated how risk-based regulation helps regulators to mitigate and manage the risks in the financial sector. Hutter provides an effective summary of risk-based regulation:<sup>139</sup> it will usually be based on a philosophical commitment to risk management principles as the governance framework that provides the regulator with the basis for how all work is undertaken.<sup>140</sup> All regulation uses 'risk-based tools emerging out of economics (for example, cost-benefit approaches) and science (for example, risk assessment techniques)'.<sup>141</sup> The regulator approaches its work as a series of ongoing cycles, commencing with an initial risk identification and then proceeding through risk measurement, mitigation and control and monitoring.<sup>142</sup>

#### **4. Addressing the arguments over the best strategy to implement regulation: Principles versus rules**

Turning now to the question of the best strategy to implement regulation, the debate has continued to develop over the course of researching this thesis to reach the latest strategy. The best strategy depends on the legal framework and cultural context as well, so what works in the UK does not necessarily work in Kuwait. However, there is agreement that a rule-based approach is not the best strategy to implement regulation.<sup>143</sup> The collapse of Barings Bank revealed the drawbacks to rule-based regulation. Undoubtedly, in seeking an efficient regulatory approach it is good practice to compare rule-based and principles-based systems to reveal the weaknesses in the rule-based approach. Rules with a specific set of procedural requirements cannot cover all the situations and difficulties that regulated firms face in

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<sup>139</sup> Bridget Hutter, 'What Makes a Regulator Excellent? A Risk Regulation Perspective' (2015) Penn Program on Regulation's Best-in-Class Regulator Initiative, 3-5. Available: <<https://www.law.upenn.edu/live/files/4719-hutter-ppr-bicregulatordiscussionpaper-06-2015pdf>> accessed 13 March 2020.

<sup>140</sup> Ibid. 3.

<sup>141</sup> Ibid. See Julia Black, 'Risk-Based Regulation: Choices, Practices and Lessons Learnt', in *Risk and Regulatory Policy: Improving the Governance of Risk* (OECD, corp. ed., 2010) 185–224.

<sup>142</sup> Bridget Hutter, above, (n 139) 4.

<sup>143</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCPD314.pdf>>> accessed 13 March 2020.

financial markets.<sup>144</sup> Rule-based regulation is found more commonly in bureaucratic organisations or systems where the regulator enforces a strict policy on the regulated firms to ensure their compliance with specific set of rules.<sup>145</sup> The interview data reveal that Kuwait still follows a rule-based approach to regulation, which has led to the CMA facing many challenges in applying a risk-based approach. This differs from principle-based regulation, which uses a broad set of principles of conduct issued by the regulator and gives more discretionary power to the regulated firms to decide how to implement the principles according to their objectives.<sup>146</sup>

The drawbacks of rule-based regulation can be summarised in three points. First, it cannot cover all the situations and risks faced by regulated firms.<sup>147</sup> In some cases there is no specific rule to apply to a given situation, which could lead to serious problems. For example, it was unclear who was responsible for supervising Nicholas Leeson at Barings. In other cases rules could conflict with each other, and there are no set standards to cover such deficiencies. The regulator is required to update the standards and procedures regularly, but experience has proved that it is extremely difficult to cover all situations. A checklist policy can help to provide comparability and standardisation, but it will not be flexible and cover all scenarios.<sup>148</sup> Secondly, implementing all rules and procedural requirements might lead to false information or statements. Meeting the letter of the law, as rule-based regulation proposes with its specific rules and procedures, may not take into account the spirit of the law.<sup>149</sup> Some rules are created in response to specific situations without taking into consideration changes in the present situation or possible changes in the future. Finally, there may be a lack of discretion in the way regulated firms apply the rules and standards.<sup>150</sup> Licensed persons tend to focus on complying with the rules regardless of whether they will achieve their objectives. It takes time and money to ensure compliance with the rules and

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<sup>144</sup> Surendra Arjoon, 'Striking a balance between rules and principles-based approaches for effective governance: A risks-based approach' (2006) 68 *Journal of Business Ethics* 53, 69.

<sup>145</sup> *Ibid.* 57.

<sup>146</sup> Mark Newey, 'What are the benefits of principle-based regulation', (Groveland, 10th June 2013), see also Julia Black, 'Principles Based Regulation: Risks, Challenges and Opportunities' (London School of Economics and Political Science, (2007) 7-9.

<sup>147</sup> Surenda Arjoon, above, (n 144) 68.

<sup>148</sup> Peter Christian Metzger, 'Macro-prudential financial regulation of banks after the crisis of 2008' (PhD thesis, University of Newcastle 2016) 63.

<sup>149</sup> Surenda Arjoon, above, (n 144) 68-69.

<sup>150</sup> Mark Newey, above, (n 146) See also Julia Black, 'Principles Based Regulation: Risks, Challenges and Opportunities', above (n 146) 9.



standards. An overemphasis on a rule-based approach can lead to a crisis such as the Barings collapse because its focus is more on ticking all the boxes than on the reality.

In this context, Black notes that the regulatory principles relied upon to construct risk-based frameworks are general rules expressing ‘the fundamental obligations that all should observe’.<sup>151</sup> For Black, principles-based regulation avoids any reliance on ‘detailed, prescriptive rules and relies more on high-level, broadly stated rules or principles’.<sup>152</sup> This is an important point when understanding why the FCA moved from a risk-based approach to forward-looking judgement. For decades before the crisis, the entire UK regulatory philosophy adopted towards the management of financial markets was reflected in the phrase ‘a light touch’.<sup>153</sup>

Moreover, principles-based regulation shifts the balance from relying on the regulator’s rulebook towards an approach which gives the regulated firm the freedom to decide how to implement the principles. There are risks and challenges associated with principles-based regulation. The fundamental issue is the uncertainty and unpredictability of a regulatory regime in which the regulator cannot act retrospectively.<sup>154</sup> The principles are not sufficient, because they are too generalised for implementation of the law. There is a need to interpret principles to enforce them, and not all the interpretation is accurate or similar.<sup>155</sup> If the regulator provides too much guidance in clarifying the principles, they become too detailed and similar to the rules-based approach.<sup>156</sup> Unpredictability prevents the industry from knowing what the supervisory and enforcement response will be.<sup>157</sup> It is important to understand that there should be three features of the regulatory responses to non-compliant firms: they should be predictable, rational and consistent. Principles-based regulation can help by facilitating coordination for well-intentioned firms to comply with the law, but it does not help with less well-intentioned firms which need more predictable rules, as in the rule-

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<sup>151</sup> Julia Black, *Principles Based Regulation: Risks, Challenges and Opportunities* above, (n 146) 3.

<sup>152</sup> Ibid.

<sup>153</sup> Cecily Rose, 'The UK Bribery Act 2010 and Accompanying Guidance: Belated Implementation of the OECD Anti-Bribery Convention' (2012) 61 *International & Comparative Law Quarterly* 485, 487-488.

<sup>154</sup> Julia Black, *Principles Based Regulation: Risks, Challenges and Opportunities*, above, (n 146) 2.

<sup>155</sup> Peter Christian Metzger, above, (n 148) 64.

<sup>156</sup> Julia Black, Martyn Hopper and Christa Band, 'Making a success of principles-based regulation' (2007) 1 *Law and financial markets review* 191, 197.

<sup>157</sup> Ibid. 196.

based approach. The UK regulatory reform committee clarifies this relationship by stating that:<sup>158</sup>

Principles-based regulation focuses both regulators and the regulated on delivering against regulatory objectives. This avoids regulation becoming an exercise in purely ‘going through the motions’ or ‘box-ticking’. Current principles-based regimes combine specific rules and general principles. The BRE [Better Regulation Executive] believes that creating this balance is the correct approach and will continue to help ensure that this is the case. It is essential that clear guidance is provided, where appropriate, to assist those regulated in understanding what is required in order to comply with regulation.

Following the Barings collapse, the UK banking system adopted a new concept of supervision and a risk-based approach to regulation. This approach helps to understand and manage public expectations about the regulatory regime.<sup>159</sup> It was believed that risk regulation could redesign the relationship between the regulator and regulated firms in terms of responsibility and supervision.<sup>160</sup> There was still uncertainty as to how to establish a framework to assess the risks that the markets faced, perhaps due to the fact that the risk-based approach is a complex process and it is unclear how to balance the market’s risks and the regulator’s objectives.<sup>161</sup> Thus it is important to understand what the risk-based approach means in the financial sector, and this is explained in the next section.

## **5. Designing a risk-based approach**

Many jurisdictions have moved away from a rigid rules-based system to rely on a more flexible and targeted strategy which take into consideration the regulator’s discretion to allocate its resources through the adoption of a risk-based approach.<sup>162</sup> The framework of a risk-based approach is explained below.

### **5.1 Risk-based framework**

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<sup>158</sup> Better Regulation Executive, ‘The Implication of the Financial Crisis for Regulation’ << <https://publications.parliament.uk/pa/cm200809/cmselect/cmdereg/329/32906.htm>>> accessed 13 March 2020.

<sup>159</sup> Joanna Gray and Jenny Hamilton, above, (n 121) 5. See also Michael Power, above, (n 122).

<sup>160</sup> Joanna Gray and Jenny Hamilton, above, (n 121) 15.

<sup>161</sup> Joseph Norton, above, (n 88) 36.

<sup>162</sup> IOSCO, ‘Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries’, (2009) 3 available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 13 March 2020.

The 2010 Bounds review of how regulatory policy is most effectively designed provides an excellent starting point for this section.<sup>163</sup> He observes that evaluating the impact of a regulatory approach without looking at its unintended consequences is unsound. It is preferable to consider whether these consequences ‘themselves are tolerable, or whether they undermine the benefits of addressing the primary risk’. While it is doubtful that any sensible person (assuming they regarded the crisis as an unintended consequence) would ever conclude that the highly negative crisis outcomes of bank failures, illiquid global capital markets and strained public confidence could be accepted as tolerable, it is suggested that Bounds accurately assumes that regulatory approaches must be examined dispassionately.

Risk-based regulation can be defined as a legal framework consisting of set of principles to prioritise regulatory actions to control and mitigate risks that affect the achievement of the regulator’s statutory objectives.<sup>164</sup> It is a strategy to allocate limited regulatory resources to focus on the highest risks posed to these objectives.<sup>165</sup> It moves away from rules-based regulation to a reliance on the regulator’s discretion to design the strategy to mitigate risk. It aims to provide early-warning signals to the regulator to pay attention to the highest-risk firms in the market.<sup>166</sup> It can be used to supervise and enforce regulations. It evaluates firms based on the impact of their risk on the regulator’s objectives, and determines the supervisory and enforcement programme to decide on off-site supervision or targeted on-site inspection.<sup>167</sup>

There are four core elements to designing a risk-based framework.<sup>168</sup> Firstly, the regulator must clarify its statutory objectives. It is extremely important that these objectives are clear, to ensure that the regulator designs its strategy to achieve them and controls any risks that might affect this. It requires the regulator to state its objectives explicitly either by rules or by act.

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<sup>163</sup> Gregory Bounds, ‘Challenges to Designing Regulatory Policy Frameworks to Manage Risks’ (OECD, 2010) 3.

<sup>164</sup> Julia Black, and Robert Baldwin, ‘When risk-based regulation aims low: Approaches and challenges’ (2012) Regulation & Governance 6.1, 2-22, 12-13 see also OECD, Summary Of Discussion on Risk and Regulation at the Meeting Of The Group on Regulatory Policy, 1-2 December 2008.

<sup>165</sup> Julia Black and Robert Baldwin, above, (n 164), 4-5.

<sup>166</sup> Bridget Hutter, ‘The Attractions of Risk-Based Regulation: Accounting for the Emergence of Risk Ideas in Regulation’ (2005) 33 Centre for Analysis of Risk and Regulation Discussion Paper, 13.

<sup>167</sup> Julia Black, ‘The Development of Risk Based Regulation in Financial Services: Canada, the UK and Australia’ (2004) ESRC Centre for the Analysis of Risk and Regulation Research Report, 18-21.

<sup>168</sup> Julia Black, ‘Risk-Based Regulation: Choices, Practices, and Lessons Learnt’ above, (n 141) 185-224, 193-195., see also Julia Black, ‘The Emergence of Risk-Based Regulation and the New Public Risk Management in the United Kingdom’ above, (n 99) 512, 514-516, see also Financial, January 2000, A New Regulator for the New Millennium.

This element is absent in Kuwait legal structure. As the interview data and economic reports reveal, there are no adopted policies and no mechanisms to enforce those objectives in Kuwait.<sup>169</sup> In addition, the unclear objectives of the CMA must be clarified to enable the risk-based approach to be applied correctly. This is discussed in detail in Chapter 4.

Second, the regulator must identify the risks to be controlled and mitigated.<sup>170</sup> This requires the regulator to use its discretionary power to decide which risks will be controlled and which will be ignored. In other words, there are many risks in financial sectors but only limited resources, so in practice the regulators cannot control and mitigate all risks. Some discretion must be used by the regulator in identifying the most significant risks. This element is also weak in the Kuwait system. The research interviews for this thesis revealed that there is no mechanism to measure risk as being high or low in the CMA. Current practice depends on policy being used randomly to supervise the most important risk. Furthermore, the CMA's annual reports do not state the policy for supervising risk in the financial sector.<sup>171</sup>

Furthermore, as noted before, it is no easy task to identify risks, especially uncertain risks.<sup>172</sup> The uncertainty factor is impossible to predict, because many situations are unique.<sup>173</sup> It means an event cannot be calculated mathematically in terms of probability and cannot be measured, so the risk cannot be controlled. It is important to identify the difference between uncertainty and risk, where risk can be measured precisely to ensure certainty in a principles-based regime, while uncertainty is impossible to predict.<sup>174</sup> Such a regime needs a level of shared understanding between the regulator and regulated firms, but there are mismatches and mindset gaps between them which can lead to breakdowns. The lack of a good understanding of the CML is one of the main weaknesses of the Kuwait legal system in applying a risk-based approach. The interview data and a workshop organised by the CMA to discuss and explain the CML showed there is lack of understanding of financial regulation.<sup>175</sup> In addition to filling these gaps, there need to be substantial changes in the skills, judgement

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<sup>169</sup> State Audit Bureau report for financial year 2017/2018 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>170</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above (n 168) 217.

<sup>171</sup> The CMA Report for the Financial Year 2018/2019 (in Arabic).

<sup>172</sup> Frank Knight, *Risk, uncertainty and profit* (Courier Corporation 2012), 199-202.

<sup>173</sup> *ibid*, 204.

<sup>174</sup> *ibid*, 204.

<sup>175</sup> The CMA's workshops << [https://www.cma.gov.kw/ar/web/cma/awarenessevents/-/cmageneric/type/awareness\\_workshops](https://www.cma.gov.kw/ar/web/cma/awarenessevents/-/cmageneric/type/awareness_workshops) >> accessed 18 March 2020.

and mindset of the regulators and regulated firms to enable a principles-based regime to be implemented efficiently.<sup>176</sup> All these are impediments to principles-based regulation.

Thirdly, after setting out objectives and identifying risks, the regulator prioritises its actions based on the level of risk against the statutory objectives.<sup>177</sup> Expert judgement is required to decide which risks need to be controlled.<sup>178</sup> In general, the regulator needs to appoint staff who are professional and experts in financial regulation to be able to analyse risk and set out regulatory priorities. This element is important, because it will be the basis of the regulator's accountability. To clarify, whatever risks the regulator decides to neglect or to avoid by mitigation or control will be questioned by the superior power which supervises the financial regulator.<sup>179</sup> There are two type of accountability, namely managerial and political.<sup>180</sup>

Managerial accountability comes from the regulator's structure and internal organisation, while political accountability comes from separation of powers and the principle of checks and balances. For example, in the UK the FCA is accountable to the Treasury; in Kuwait the CMA is accountable to the Ministry of Commerce and Industry (MOCI). Thus it is important to clarify the legal basis for the prioritisation policy the financial regulator will adopt, which is based on the level of risk to affect the achievement of the statutory objectives.

Finally, the regulator allocates its resources to control and mitigate the high-impact risks to its statutory objectives. This is the whole purpose of the risk-based approach to regulation: it deploys limited resources to manage unlimited risk.<sup>181</sup> Effective resource distribution helps to provide an efficient framework to supervise and enforce financial regulation.

Another important element is data collection and management.<sup>182</sup> The key to efficient risk-based regulation is the collection and analysis of information relevant to the market, firms

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<sup>176</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 197

<sup>177</sup> Bridget Hutter, above, (n 166) 2-3.

<sup>178</sup> Robert Baldwin and Martin Cave, 'Understanding Regulation: Theory, Strategy, and Practice' (Oxford University Press, 2012), 100 Joanna Gray and Jenny Hamilton, above, (n 121) 38.

<sup>179</sup> Eva Hüpkens, Marc Quintyn and Michael Taylor, above, (n 16) **Error! Bookmark not defined.** 8-12

<sup>180</sup> Ligia Catherine Arias Barrera, 'Fractures of the UK regulation and supervision of Central Counterparties in the OTC Derivatives Market' (PhD thesis: University of Warwick, 2016) 55.

<sup>181</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 13 March 2020.

<sup>182</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) see also Ligia Catharine arias barrera, above, (n 180) 45.

and any other factors related to financial markets. If the regulator has broad access to data and information, the framework of risk-based regulation will be efficient.

The UK FSA announced its adoption of a risk-based approach in a 2000 paper, 'A New Regulator for a New Millennium',<sup>183</sup> whereas Kuwait adopted risk-based regulation after the 2008 financial crisis and is still in a process of understanding and enforcing this system in the financial sector.<sup>184</sup> There are some concerns about applying risk-based financial regulation. For example, Breyer criticised this approach on three grounds: overregulation, random selection of priorities and inconsistent implementation.<sup>185</sup> These factors are all found in the Kuwaiti system. The fieldwork shows there are too few experts, and they do not have the experience to develop a coherent risk framework. Above all, there is an absence of public information about the risk-based approach and its implementation.

The precondition to applying a risk-based approach is an understanding of the philosophy of this approach, and working together with the industry to apply the approach correctly. The current situation in the CMA and the financial sector reveals a lack of knowledge of the risk-based approach and its application. Six out seven research interviewees said they are unaware of the risk-based approach and its application in the CMA; only Participant No. 1 had any idea of the risk-based approach:

The policymakers did not adopt any approach to regulate financial regulation. There is no published policy about the purpose of the law. In fact, most of the articles are adopted/copied from other jurisdictions. Risk-based approach is a new definition to Kuwait financial sector. The CMA is in the process to adopt it because the Capital Adequacy regulation stated its adoption risk-based approach as basis of these regulations.

Other participants were unaware of the approach. Participant No. 2 stated:

There is no risk-based approach to regulate the financial regulation. The law is adopted from English and US laws to regulate the financial sector. The 2015 amendments were based on organised campaign to change the law to achieve private interest affected by the strict regulation dealing with insider trading and market manipulation, specially article 122. The stock markets faced shortage in term of liquidity, which led investors to not strictly follow the law against the manipulator, to allow some illegal activities and movements in the stock market. They called market manipulators as the 'salt of the markets'. The CMA did not

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<sup>183</sup> Financial Service Authority, 'A New Regulator for a New Millennium' (2000)

<sup>184</sup> Julia Black and Robert Baldwin, 'Really Responsive Risk-Based Regulation' (2010) 32 Law & Policy 181, 15

<sup>185</sup> Stephen Breyer, *Breaking the Vicious Circle: Towards Effective Risk Regulation* (Harvard University Press, Cambridge MA, 1993).

adopt the risk-based approach as the basis of their regulation and there is no publication nor clarification about this approach.

Participant No. 3 stated:

Of course, there is no public policy about the CML and its Executive Bylaws. No one knows what risk-based approach really means. Most of CMA law is adopted from US and UK laws. In fact, there are unusual articles that have been copied and pasted from UK laws regarding acquisition.

Participant No. 4 stated:

There is no public policy in terms of the purpose of the law. It is vague as what does the law achieve, what is the purpose of the law. The question is: does it protect the markets? Or the investor? The ordinary investor or foreign investor? To evaluate the law, we need to understand the purpose of the law and what does the law achieve. There is no such clarification in terms of the purpose of the law at all. This makes the researcher wonder and question the ability of the law.

Participant No. 5 stated:

The CML did not adopt any policy and no clear purpose of the law. On the contrary, the CMA Executive Bylaws are tailored to adopt the best practice according to IOSCO standards. The Executive Bylaws amendments will not be issued until the industry comments on the law and studies its impact on the markets.

Participant No. 6 stated:

There is no adopted policy in regulating financial regulation in Kuwait. It is simply a law that is a reaction of the 2008 crisis. In fact, the financial regulations have been transplanted from other jurisdiction like Saudi Arabia and they translated theirs from the UK and the US as well. Risk-based approach is new approach that the CMA has not mentioned in their annual review or in public statement.

Despite this lack of knowledge, currently there is a serious move towards a risk-based approach as a basis for regulation in the CMA, as Participant No. 1 confirmed. The initial step was a request by the CMA to licensed persons to submit a report about sound systems, risk management and internal audit, with a submission deadline of 30 June 2019. The purpose of these reports is to allow the CMA to prepare an assessment of licensed persons' risks in financial sectors. There is much to be done to apply risk-based regulation in Kuwait, but at least there is movement in this regard.

## 5.2 Risk assessment

There are unlimited risks in the financial sector, hence each risk must be assessed to evaluate it and set out the regulator's priorities accordingly.<sup>186</sup> Black suggests focusing on three areas to create the risk assessment: impact and probability; weighting; and integrating horizon scanning and generic industry-wide risk assessment into the firm-specific assessment.<sup>187</sup> Risk assessment can capture both qualitative and quantitative risks in financial markets.<sup>188</sup> While the qualitative risks can be identified as human resources, administrative, systemic and compliance, the quantitative risks are financial, markets and operational.<sup>189</sup> The important point is how the financial regulator makes risk assessments.

Firstly, the impact and probability of risk in the financial sector explore how the regulator assesses the risks to analyse each correctly. Under a risk-based approach one of the important steps and the most difficult tasks is to identify risk, because there are measurable and non-measurable risks. For measurable risk, the regulator must evaluate the risk impact or probability, weight the impact or probability and create some balance to assess risks. The regulation of risk should be based on an assessment of the events and activities of a firm, recognising the firm's size and funds as the basis for impact measures.<sup>190</sup> It is basically the risk's impact on the regulator's statutory objectives which dictates the regulatory appetite for such risk. To clarify this concept, the regulator categorises risks depending on their impact in achieving its objectives. In the UK the regulator has three categories in its risk framework, namely low-impact firms, medium-low firms, and medium-high and high-impact firms.<sup>191</sup> Each category is subject to different assessment by the regulator in evaluating the nature of the harm that the firms pose to the achievement of the statutory objectives.

Second, it is significant that the regulator weights the risks, giving more attention to certain risks than others, and works accordingly. The regulator devotes its resources to managing and controlling risks which might affect the statutory objectives, so there is a mechanism to weight risks and give them different scores based on the risk level. It presents the regulator's

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<sup>186</sup> The financial regulators do not publish risk assessment, largely out of concern that they will be misunderstood by the public and damage the market confidence. (Julia Black, OECD, 2010).

<sup>187</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 196.

<sup>188</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) 14 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 13 March 2020.

<sup>189</sup> *ibid.*

<sup>190</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 196.

<sup>191</sup> FSA, 2006 see also Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 197.



view of risk. The risk level is important in helping the regulator to protect the market, so the regulator divides the risks into important (which it will prepare for) and non-important. The responsibility for non-important risk still lies with the regulator, which may lead to accountability if the regulator ignores such risks. The final score of risks is the result of calculating the potential and measurable risk of firms against the regulatory objectives. This score leads to firms' risk profile to guide the regulator to devote its resource and supervision power to the highest risk profiles.<sup>192</sup> Furthermore, as Black states, there are three reasons for weighting: 'incentivising management; structuring supervisors' risk assessments; and structuring charges'.<sup>193</sup>

Finally, integrating horizon scanning and generic industry-wide risk assessment into a firm-specific assessment draws in risks that are not included in the balance sheet or books, but relate to the environment in which the firm operates. Some risks are not within the firm's scope of work, but the firm is affected because it is part of the market. The regulator considers these risks when designing the risk framework. Industry risks can be analysed and evaluated as part of the firm-specific assessment to create an efficient risk-based framework.

### 5.3 Drawbacks of risk-based regulation

In essence, the 2008 financial crisis was the result of an increasing willingness on the part of international financial markets (including large banks and other financial services market players) to assume risk in pursuit of ever-greater rewards.<sup>194</sup> The collapse of the US subprime mortgage markets in late 2006 (the widely accepted trigger for the crisis that quickly unfolded) is an excellent example of how the appetite for risk increased in markets where regulatory oversight was not sufficient to provide any effective counterbalance.<sup>195</sup> The Northern Rock bank collapse is another example that proved there were limitations in the ability of risk-based regulations to protect financial markets (see Chapter 1.2,

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<sup>192</sup> FSA, 2006 see also Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 198.

<sup>193</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Learnt' above, (n 168) 200.

<sup>194</sup> Tom Bangay 'Financial crisis: the moral of the story' (2013) Jun/Jul *International Bar Association Global Insight* 19, 20, 23-24. Available at << <https://www.ibanet.org/Article/NewDetail.aspx?ArticleUid=7EF920CA-9A29-402A-AE0B-451BC4DB5105>>> accessed 13 March 2020.

<sup>195</sup> Otakar Hajek, above, (n 113) 4. See Bank for International Settlements (BIS) (2016). The syndicated loan market. [Online] Available: <[http://www.bis.org/publ/qtrpdf/r\\_qt0412g.pdf](http://www.bis.org/publ/qtrpdf/r_qt0412g.pdf)> accessed 13 March 2020.

Background).<sup>196</sup> The incorrect calculation of risk failed to protect the regulator's statutory objectives.<sup>197</sup>

In the US subprime market, low interest rates and high returns generated by seemingly attractive mortgage-backed financial products had encouraged a lackadaisical regulatory attitude. In effect, as these products became more complex in their structure, less regulatory attention was directed at whether the underlying assets ('pools' of US residential home mortgages) were being properly appraised.<sup>198</sup> Without proper valuations, it is now obvious that if mortgage interest rates climbed (as they did in the US by late 2006), there would be an increase in mortgage defaults, thus compromising the entire investment value.<sup>199</sup>

As a result, some of the world's leading financial institutions, such as Wall Street powerhouses Lehman Brothers and Bear Stearns, which had committed large resources to these now badly flawed financial products, became overexposed and ultimately collapsed.<sup>200</sup> The global financial markets came perilously close to destruction through the ripple effects attributed to these market events with their roots in the commitment to risk-based regulatory environments.<sup>201</sup>

Furthermore, risk-based regulation cannot provide a proactive strategy to protect the markets. In some cases the most important risks are neglected.<sup>202</sup> Under a risk-based approach, entities are risk rated in accordance with their previous actions and the impact of their non-compliance. These factors may mislead the regulators supervising the entities, and not reflect the truth about each entity. These problems of the risk-based approach can affect the regulators' performance in protecting markets, and they may not be able to achieve their

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<sup>196</sup> Joanna Gray, above (n 106) 52.

<sup>197</sup> It is important to clarify that the FSA never use term 'light-touch' to describe its policy or regulation. see Iain MacNeil, 'An Introduction to the Law on Financial Investment', Oxford and Portland, Oregon, 2012) 105, see FSA, 'The Turner Review, A Regulatory Response to the Global Banking Crisis' (March 2009) available at << [http://finra.complinet.com/net\\_file\\_store/new\\_rulebooks/f/s/FSA\\_at\\_slides.pdf](http://finra.complinet.com/net_file_store/new_rulebooks/f/s/FSA_at_slides.pdf)>> accessed 13 March 2020.

<sup>198</sup> Alexandra Kastrinou, 'The thin line between corporate rescue and state aid: an overview of the impact of state aid rules on the banking sector' (2014) 25(10) *International Company and Commercial Law Review* 356, 359.

<sup>199</sup> Ibid.

<sup>200</sup> House of Commons Treasury Committee, 'The run on the Rock', Fifth Report of Session 2007-08, Vol. I (January 2008), 2-5.

<sup>201</sup> Ibid.

<sup>202</sup> Julia Black and Robert Baldwin, 'Really Responsive Risk-Based Regulation' (2010) 32 *Law & Policy* 181. See International Monetary Fund, 'United Kingdom- Basel Core Principle for Effective Banking Supervision Detailed Assessment of Compliance United Kingdom' (August 2011) available << <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/United-Kingdom-Basel-Core-Principles-for-Effective-Banking-Supervision-Detailed-Assessment-25125>>> accessed 13 March 2020.

objectives as the result of an inaccurate picture of the markets and the regulated firms which does not reflect the reality and the hazards that the markets might face. Sometimes the regulator is unable to ensure an accurate assessment in terms of the generic risk and its effect on the statutory objectives.<sup>203</sup> It is difficult to achieve flawless risk assessment because it depends on the regulator's judgement or discretion to analyse a risk. Thus there are challenges in the implementation of a risk-based approach.

First, collecting and analysing data and information to rank the regulated firms is expensive and requires intensive resources.<sup>204</sup> It takes a considerable amount of work by the regulators and regulated firms to analyse the information accurately.

Secondly, there is no uniform methodology to assess and analyse the risk for each regulated firm.<sup>205</sup> This leads to the question of what type of risk the regulator should focus on and whether to focus on certain types of risk or firms and at what level of the industry.<sup>206</sup> Experience has shown that regulated firms can face huge and different types of risks, which necessitates an expert to prioritise each risk and also absorbs considerable resources.<sup>207</sup> Thus it is important to have a specific methodology to address each area of risk.

Finally, the social context is important to enforce risk-based regulation.<sup>208</sup> It requires awareness of the importance of risk-based regulation and its application in financial services.<sup>209</sup> Firms must recognise a risk-based approach to be able to design the framework.

Kuwait still uses rule-based regulation for financial services and stock markets, but recently there is some movement towards adopting risk-based regulation. As the above analysis shows, the neglect of some risks can lead to financial crisis, so there is a need for expert staff to measure risks and allocate resources. The fieldwork showed that to date there is an absence of understanding of the risk-based approach. This might result in incorrect application of the approach, leading to the problems the UK financial regulator faced during the supervision of Northern Rock. Kuwait is way below the UK in regulatory experience and knowledge, and

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<sup>203</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Leant' above. (n 168) 201.

<sup>204</sup> Ibid., 203.

<sup>205</sup> Eric Windholz, *Governing Through Regulation: Public Policy Regulation and the Law* (Routledge 2017) 254.

<sup>206</sup> Julia Black, 'Risk-Based Regulation: Choices, Practices, and Lessons Leant' above, (n 168) 201.

<sup>207</sup> Ibid. 220.

<sup>208</sup> Ibid. 220.

<sup>209</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) 22 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 18 March 2020.

the UK regulator failed to apply the approach correctly despite all its expertise. Thus the CMA must take cautious and slow steps towards adopting a risk-based approach. It is also important to understand why the CMA is focusing on a risk-based approach as its newest strategy to regulate markets, and not a judgement-led approach.

## **6. The adoption of forward-looking judgement-based regulation**

It is notable that the financial crisis prompted a wide range of legislative enactments and market regulatory policies; these confirm both the seriousness of the market impacts of the crisis and a collective international commitment to prevent any future crisis occurring.<sup>210</sup>

In the post-crisis period in the UK, on 1 April 2013 the FCA took over responsibility for conduct and relevant prudential regulation from the FSA.<sup>211</sup> The FCA assumed primary responsibility for all UK market rules enforcement, supervisory measures and determination of any necessary remedial actions at any given time. When these various responsibilities are reduced to a single FCA purpose, it seems that in the crisis aftermath the FCA sought to demonstrate that the new UK approach to market regulation, as explained below, can be trusted more than its pre-crisis risk-based market supervision and oversight. It is suggested here that the extent to which any market regulatory approach actually encourages market institutions and broader public trust is likely the soundest indication of whether the regulation is effective.<sup>212</sup>

A more general issue arises in this context – one that bears directly on any final assessment of whether the FCA’s commitment to judgement-based regulation will ultimately prove more effective than the pre-crisis approach. A literature review indicates that there is a major contemporary debate concerning behaviour modification and the relative merits of deterrence versus compliance regimes.<sup>213</sup> It is suggested that ‘behaviour modification’ is a useful

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<sup>210</sup> Bank for International Financial Settlements (BIS) ‘History of the Basel Committee’ (2016) Available: <<http://www.bis.org/bcbs/history.htm>> Accessed 22 January 2020

<sup>211</sup> The Financial Service Act 2012 the amendment of the Financial Services and Markets Act 2000. See Financial Conduct Authority ‘The FCA’s approach to advancing its objectives’ (2015) Available: <<https://www.fca.org.uk/publication/corporate/fca-approach-advancing-objectives-2015.pdf>> accessed 22 January 2020.

<sup>212</sup> HM Treasury, A new approach to financial regulation: Judgement, focus and stability (HMSO, 2010), 2-8.

<sup>213</sup> A point taken from Professional Standards Authority (PSA) ‘Risk in regulatory policy 2015: Review of the literature’ (2016) 17 [Online] Available: <<https://www.professionalstandards.org.uk/docs/default-source/publications/research-paper/risk-in-regulatory>> accessed 22 January 2020.

alternative way to describe the FCA regulatory principle of how to encourage firms to ‘do the right thing’.<sup>214</sup>

McGivern notes (in a non-financial context) that deterrence regimes rely on the ‘application of sanctions or penalties to the few to encourage compliance of the many’.<sup>215</sup> Conversely, compliance regimes tend to emphasise a ‘more collaborative relationship between regulator and regulated’, with a stress on ‘diplomacy, persuasion, or education’.<sup>216</sup> Returning to the literal meaning of the FCA principles embodied in its regulatory framework, the repeated emphasis on intervention and robust responses to apparent market supervision issues is highly suggestive of deterrence in action. However, the FCA commitment to encouraging market players to comply has a collaborative element.

### 6.1 Judgement-based regulation

The drawbacks of the risk-based approach form an effective foundation to explain the FCA’s move towards a judgement-led approach.<sup>217</sup> As noted, risk-based regulation must be contrasted with the current FCA commitments to more forward-looking regulatory approaches.<sup>218</sup> The FCA summarises its philosophy in the following fashion: ‘a pre-emptive approach’ based on ‘forward-looking judgement’ or ‘judgement-led regulation concerning financial market firms’ business models, product strategy and how they run their businesses, to enable the FCA to identify and intervene earlier to prevent problems crystallising’.<sup>219</sup> As the FCA published guidance clearly confirms, this new framework equipped UK regulators to link regulatory theory better with effective practice.

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<sup>214</sup> The FCA, ‘Transforming Culture in Financial Service’ available at <<<https://www.fca.org.uk/publication/discussion/dp18-02.pdf>>> accessed 22 January 2020.

<sup>215</sup> Gerry McGivern, Michael Fischer, Tomas Palaima, Zoey Spendlove, Oliver Thomson and Professor Justin Warin, ‘Exploring and explaining the dynamics of osteopathic regulation, professionalism and compliance with standards in practice’ (2015) Available: <http://www.osteopathy.org.uk/news-and-resources/document-library/research-and-surveys/dynamics-of-effective-regulation-final-report/> accessed 13 March 2020.

<sup>216</sup> Ibid.

<sup>217</sup> See: (i) *Economist*, ‘Crash course: the origins of the financial crisis’ (2013) [Online] Available: <<http://www.economist.com/news/schoolsbrief/21584534-effects-financial-crisis-are-still-being-felt-five-years-article>> [22 January 2020]; (ii) John Duca, ‘How and Why the Crisis Occurred’ (2014) Federal Reserve Available: <<http://www.federalreservehistory.org/Events/DetailView/55>> [22 January 2020]; (iii) Julia Black, ‘The Development of Risk Based Regulation in Financial Services: Canada, the UK and Australia above, (n 158)

<sup>218</sup> Regulatory Reform Committee ‘Regulatory Reform Committee - Ninth Report: Themes and Trends in Regulatory Reform’ (2009) [Online] Available: <https://publications.parliament.uk/pa/cm200809/cmselect/cmdereg/329/32902.htm> accessed 13 March 2020.

<sup>219</sup> Financial Conduct Authority ‘The FCA’s approach to advancing its objectives’ (2015) Available: <<https://www.fca.org.uk/publication/corporate/fca-approach-advancing-objectives-2015.pdf>> accessed 13 March 2020.

The FCA has published principles that provide the foundation for its regulatory regime. The principles give an excellent indication of how far the FCA has moved from the UK pre-crisis financial markets regulatory philosophy: ‘forward looking and more interventionist’; ‘focused on the big issues and causes of problems’; ‘viewing poor behaviour in all markets through the lens of the impact on consumers’; and ‘orientated towards firms doing the right thing’.<sup>220</sup>

The FCA judgement-led regulation commitments have invited significant academic attention, as explained below. However, it is useful initially to consider the literal meanings that are attached to each of those principles, as a means of establishing the extent to which UK market regulation has moved towards a judgement-led approach.<sup>221</sup>

In contrast to the risk-based approach and its emphasis on the initial risk identification, measurement, mitigation, control and monitoring ‘cycles’ explained above,<sup>222</sup> the FCA’s forward-looking judgement approach is inherently proactive. The FCA does not confine itself to identifying market risks and then providing oversight as these risks define the appropriate regulatory scope. Instead, an active, interventionist FCA presumes a regulator is keen to seek out and (where possible) negate market problems before they have the opportunity to grow into a market contagion.<sup>223</sup> One could argue that an overly active, interventionist regulator might unduly interfere in market functions. The counter argument is more attractive when placed in the post-crisis contexts in which the FCA now operates: the crisis events required active prevention, and the current FCA regulatory scheme appears to achieve this outcome.

Similarly, the stated FCA focus directed at ‘big issues and causes of problems’ is consistent with the need on the FCA’s part to provide permanent regulatory solutions, as opposed to temporary ones.<sup>224</sup> The FCA principle of consumer orientation is also consistent with the public trust points emphasised above. The crisis, including its related bank nationalisations

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<sup>220</sup> Ibid, 10 principles.

<sup>221</sup> Professional Standards Authority (PSA) ‘Risk in regulatory policy 2015: Review of the literature’ (2016) Available: <<https://www.professionalstandards.org.uk/docs/default-source/publications/research-paper/risk-in-regulatory>> accessed 13 March 2020.

<sup>222</sup> Bridget M. Hutter ‘What Makes a Regulator Excellent? A Risk Regulation Perspective’ (2015) Pennsylvania University Available: <https://www.law.upenn.edu/live/files/4719-hutter-ppr-bicregulatordiscussionpaper-06-2015pdf> accessed 13 March 2020.

<sup>223</sup> The phrase used in numerous crisis contexts, such as Organisation for Economic Co-operation and Development (OECD), *Corporate Governance and the Financial Crisis -- Key Findings and Main Messages* (2009), <<http://www.oecd.org/dataoecd/3/10/43056196.pdf>> accessed 13 March 2020.

<sup>224</sup> Travers Smith, ‘FCA and PRA enforcement actions: themes and trends’ (2017) 148(Jul) *C.O.B.* 1, 34.

and severe shocks to public confidence, could be characterised from a mainstream public perspective as entirely preventable if (to paraphrase a prevailing public sentiment) ‘the UK government and its regulators had been doing their jobs’.<sup>225</sup> It is argued that the UK public could fairly conclude that risk-based regulation ‘signally failed to protect consumers and the public from the catastrophic failure of the banking system’.<sup>226</sup> For the public, the ability to trust whatever the FCA initiates regarding market oversight becomes the single most important issue in this post-crisis period.

The words ‘orientated towards firms doing the right thing’ are at least suggestive of an FCA that might seek to encourage good market behaviour, as in the philosophy explained above, versus the otherwise robust tone the FCA principles appear to impress upon their reader.<sup>227</sup> In other words, the FCA policies are sufficiently flexible to encourage market participants to pursue sound business policies proactively, without always using sanctions to achieve effective regulatory outcomes.

The regulator is not limited to examining a regulated firm’s or individual’s ‘behaviour, attitude and culture’;<sup>228</sup> rather, the regulator must carefully take into account institutional environments where regulation is being imposed. In this way, the regulator is able to assess how different control measures interact, as well as evaluating how well the regulatory measures are performing in practice. This approach thus includes the regulator identifying any measures occurring in ‘regulatory priorities, challenges and objectives’.<sup>229</sup> The approach is a consistent and positive extension of the robust, more interventionist post-crisis FCA regime detailed above. The next section establishes an understanding of how the forward-looking judgement approach helps to oversee the financial markets in the UK; prior to that, an example assists in appreciating the extent to which the FCA regulatory approach satisfies deterrence and collaboration objectives.

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<sup>225</sup> A point suggested by reading Herbert Smith, ‘Court of Appeal rejects challenge to the compensation scheme for former shareholders of Northern Rock’ (2009) << <https://www.lexology.com/library/detail.aspx?g=b2f146bd-8046-463c-ba1b-1cb47f348804>>> accessed 13 March 2020.

<sup>226</sup> Julia Black and Robert Baldwin, ‘Really Responsive Risk-Based Regulation’ (2010) 32 Law & Policy 1812.3.

<sup>227</sup> Cecily Rose, above, (n 153) 487-488.

<sup>228</sup> Ibid.

<sup>229</sup> Ibid, 3. Julia Black and Robert Baldwin, ‘Really Responsive Risk-Based Regulation’ above (n 226).

### 6.1.1 *Macris v Financial Conduct Authority* (2017)

The recent (2017) Supreme Court decision in *Macris v Financial Conduct Authority* indirectly provides an interesting basis on which to assess how the FCA regulatory attitudes are perceived and judicially interpreted.<sup>230</sup> The Supreme Court reasons are described here as an ‘indirect’ insight because the narrow issue with which the Court was concerned is not one that is immediately recognised as mainstream financial market regulation.

The applicant, a JP Morgan Chase Bank chief investment officer (CIO), claimed he had an individual right (separate from the Bank) to make submissions to an FCA investigation that concerned trading losses alleged to have resulted from this CIO’s high-risk trading strategy, weak management and an inadequate response to information available that ought to have meant the trades should never have been made.<sup>231</sup> The CIO objected to the way in which the FCA published notices issued with respect to this investigation (where over £137m was alleged to have been lost in bad trades), as the notices enabled him to be identified personally. He equated the FCA actions as akin to defamation.<sup>232</sup>

The positive contribution to this comparative assessment is not the case outcome, but rather the Supreme Court comments regarding the FCA and its regulatory commitment to the public interest. The Court held that when the FCA decided to publish its notices, these actions were entirely consistent with its obligation to ‘serve the public interest in the proper performance of its functions and the protection of those who used the financial services industry’.<sup>233</sup> The Court reached the conclusion that the public at large is entitled to know that the FCA had made this particular investigative finding, and whether a specific sector of the public might possess additional information enabling them to identify a third party (the CIO) was a less important consideration.<sup>234</sup>

In this albeit indirect way, the Supreme Court attached greater importance to the public interest in knowing what the FCA did in its investigation than to protecting the private interests (personal reputation) of this CIO. Without mentioning the specific FCA principles, or any of the above noted deterrence versus collaborative encouragement arguments, two

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<sup>230</sup> *Macris v Financial Conduct Authority* [2017] UKSC 19; [2017] 1 W.L.R. 1095 (SC).

<sup>231</sup> *Ibid.*, [4], [6].

<sup>232</sup> *Ibid.*, [11], [17].

<sup>233</sup> *Ibid.*

<sup>234</sup> *Ibid.*, [20], [24].



conclusions can be logically taken from *Macris v Financial Conduct Authority*. (It is noted in passing that as this is Supreme Court ruling, it is highly likely that these observations will be reflected in future judicial review of any similar issues.)

The first conclusion is how well aligned the Court's reasons are with the stated FCA 'robust intervention' approach. The Court gives implicit sanction to the notion that if personal reputations are called into question when the FCA pronounces upon a specific regulatory matter, the public's right to know (akin to the FCA 'consumer perspective' principle) will prevail.<sup>235</sup>

Secondly, *Macris v Financial Conduct Authority* appears to endorse the FCA actions in this case as being consistent with a deterrent financial markets regulatory approach. This argument is based on the common-sense observation that where a regulator publicises all details concerning its investigative findings, it seeks to discourage like-minded individuals or firms from engaging in similar conduct.

When these two *Macris v Financial Conduct Authority* conclusions are collectively appraised, the FCA appears to have fully embraced the new 'forward-looking' interventionist approach. In this way the Supreme Court has contributed to the likely future success of this FCA approach. The Court's approval of FCA actions will logically encourage the FCA to continue on its present regulatory path, which is a significant improvement over its former risk-based philosophies.

This case showed insight and deep understanding of the purpose and aims of the law, and the financial regulator's role in achieving those aims. As noted by six of the research participants, Kuwait does not state or clarify the purpose of its regulatory law, and the regulator cannot apply a judgement-led approach if this is not clear. The discretionary power of the financial regulator must be based on a good understanding of the meaning of the regulation; if this is absent, it is impossible to apply a judgement-led approach.

## 6.2 Elements of judgement-based regulation

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<sup>235</sup> See also *Financial Conduct Authority v Grout* [2018] EWCA Civ 71 (CA (Civ Div)), *Macris v Financial Conduct Authority*.

Judgement-based regulation shifts the language of viewing the risk to more forward-looking judgement, to include uncertainty and unknown future risk.<sup>236</sup> It is basically a strategy to exercise judgement about risk that might pose harm to the regulatory objectives, including safety, soundness and stability. So a judgement-based strategy can overcome the shortcomings of risk-based regulation in term of capturing future risks. To apply judgement-based regulation, the financial regulators must have access to information and expertise. As Gray and Peter state, there are three main obstacles to a judgement-based regime which are people, data challenges and contestability of judgment,<sup>237</sup> and these must be overcome to adopt a judgement-led approach to supervising and enforcing regulation.

This thesis analyses the CMA's capability to overcome these obstacles.

### 6.2.1 Structure

The UK–Kuwait regulatory comparison is interesting on another level. While the UK markets are arguably as sophisticated as any in the world, the CMA was created amid what AlKharafi and AlHaroun describe as a primitive Kuwait capital markets infrastructure.<sup>238</sup> This structural problem was 'coupled with the hasty, unplanned enactment of the law, led to inevitable obstacles preventing a smooth transition into the new regulatory framework and resulted in its rigid impractical application'.<sup>239</sup> It is apparent that the CMA led a speedy transition from this early regulatory chaos to present-day stability, as the interviews data strongly suggest.

The most important CMA regulatory policy shift is acknowledged in widespread academic agreement that the CMA approaches its tasks a reasonably fair and even-handed manner. Alfraih and Almutawa note that Kuwait, 'a relatively open economy with an emerging capital market', is striving to develop its economy and improve its business environment and accounting practices.<sup>240</sup> The CMA is an obvious key component in this national initiative.

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<sup>236</sup> Joanna Gray, and Christian Metzger Peter. "Defining and delivering judgement-based supervision: The interface with the legal system." *Journal of Banking Regulation* 14, no. 3-4 (2013): 228-240, 228-240.

<sup>237</sup> Ibid. 231-236.

<sup>238</sup> Abdullah AlKharafi and Abdullah AlHaroun, above, (n 38) 225.

<sup>239</sup> Ibid 221.

<sup>240</sup> Mishari M. Alfraih and Abdullah M. Almutawa 'Voluntary disclosure and corporate governance: empirical evidence from Kuwait' (2017) *International Journal of Law and Management*. 217, 236. See Mishari Alfraih, Mishari and Abdullah M. Almutawa. 'Firm-specific characteristics and corporate financial disclosure: Evidence from an emerging market.' (2014): *International Journal of Accounting and Taxation* 55-7.

The structure of the CMA must give a clear framework to allow using discretionary power to judge any risk that the CMA faces. There are currently no published details of an adopted policy on regulation,<sup>241</sup> and the interview data support the lack of a policy. The judgement-led approach must be adopted and announced by the CMA as its policy on regulation.<sup>242</sup> It needs to explain and clarify to the markets how it will exercise its power to use this approach. The lack of certainty in adopting a clear stance affects the implementation of a judgment-led approach; this contrasts with the situation in the UK, where there are public statements confirming the regulator's adoption of a judgement-led approach as the basis for supervising the financial sector.<sup>243</sup>

Of the seven financial experts interviewed, six had no knowledge of the forward-looking judgement approach to regulation. The only person who knew about it was Participant No. 1:

Kuwait can't follow a judgement-led approach because it follows the literal of law which is a Latin system not Anglo-Saxon.

This statement shows there is misunderstanding of the judgement-led approach to regulation, hence the current structure does not support the adoption of such an approach.

### 6.2.2 People

The key element of judgement-based regulation is the cultural context and the ability of the regulators to exercise judgement based on reason.<sup>244</sup> It requires a very high level of expertise by people who understand the market and its risk, and are able to see the big picture of regulation.

After the IMF recommendations of April 2019,<sup>245</sup> the CMA took steps to adopt a risk-based approach to regulation which requires expertise in the field to be able to assess risk. To go

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<sup>241</sup> Abdullah AlHayyan and Moahamad AlMutari, above, (n 68). 290.

<sup>242</sup> Joanna Gray and Christian Metzing Peter, above, (n 236) 232

<sup>243</sup> Economist, 'Crash course: the origins of the financial crisis' (2013) [Online] Available: <<http://www.economist.com/news/schoolsbrief/21584534-effects-financial-crisis-are-still-being-felt-five-years-article>> accessed 13 March 2020; (ii) John Duca, 'How and Why the Crisis Occurred' (2014) Federal Reserve [Online] Available: <<http://www.federalreservehistory.org/Events/DetailView/55>> accessed 13 March 2020 ; (iii) Julia Black, 'The Development of Risk Based Regulation in Financial Services: Canada, the UK and Australia - A Research Report' (2005) Available: <<http://www.lse.ac.uk/law/people/academic-staff/julia-black/Documents/black19.pdf>> accessed 13 March 2020.

<sup>244</sup> Joanna Gray and Christian Metzing Peter, above, (n 236) 236.

<sup>245</sup> International Monetary Fund, 'Kuwait: Financial System Stability Assessment – Update' (Report No. 19/96, April 2019) <<<https://www.imf.org/en/Publications/CR/Issues/2019/04/02/Kuwait-Financial-System-Stability-Assessment-46730>>> accessed 13 March 2020. 4.

further and adopt a strategy based on judgement is a jump to a vague world based on the CMA's knowledge and expertise. All interviewees confirmed that the CMA has not stated its policy, and without knowledge of CMA policy or information about how CMA staff will be trained to adopt the judgement-led approach, it cannot be applied correctly. Poor judgement or insufficient attention to certain risks might lead a regulated firm to collapse without the regulator taking adequate measures to protect the market, like the Royal Bank of Scotland (RBS) collapse in the UK in 2008. One of the major reasons why RBS collapsed was the inadequate assessment of risk, which led the bank to take excessive risk.<sup>246</sup> With the current limited resources of the CMA it is difficult for it to handle very risky decisions.

In Kuwait there are deficiencies in expertise and awareness about the judgement-led approach in particular, and financial regulation in general.<sup>247</sup> All participants confirmed that the CMA staff do not have the expertise to adopt a judgement-based approach. It is dangerous to adopt a new approach to financial regulation when the sector has only recently turned to a risk-based approach, and it is clear that the CMA is not ready to adopt the more developed judgement-led approach. The regulator's staff must be able to understand a firm's business and use their own judgement to assess the risk and take the necessary action,<sup>248</sup> so the success of the approach depends on the expertise of the regulator's staff.<sup>249</sup> As there is currently no knowledge or understanding of the judgement-led approach in the Kuwaiti financial sector at all, the CMA must recruit qualified staff to use the new approach (see Chapter 4).

The participants in the interviews highlighted the industry shortage of experts in financial law and lack of knowledge about the latest best practice, including the judgement-led approach. They felt that the current education system does not produce qualified employees in the financial sector.

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<sup>246</sup> Financial Service Authority Board Report, 'The Failure of the Royal Bank of Scotland' (2001) << <https://www.fca.org.uk/publication/corporate/fsa-rbs.pdf>>> accessed 13 March 2020.

<sup>247</sup> Abdullah AlHayyan and Moahamad AlMutari, above, (n 68) 500. see also Faisl Al-Haidar, 'Whistleblowing in Kuwait and UK against corruption and misconduct' (2018) 60 International Journal of Law and Management 1020, 1022. See also Mohamad Almutairi, above, (n 24) 302.

<sup>248</sup> Eilis Ferran, 'The Reorganisation of Financial Services Supervision in the UK: An Interim Progress Report' (2011) 49 University of Cambridge Faculty of Law Research Paper, 12-14.

<sup>249</sup> Nikoletta Kallasidou, 'The United Kingdom's Response to Crisis: A Critical Examination of the New Regulatory Structure of Financial Services Supervision' (2013) Bristol Law Review 117, 129. see also Treasury Committee, Financial Regulation: a preliminary consideration of the Government's proposals (House of Commons 2010-11, 430-I) << <https://publications.parliament.uk/pa/cm201011/cmselect/cmtreasy/430/430i.pdf>>> accessed 18 March 2020.

Participant No. 1 stated:

There is no course in private law schools or Kuwait University to teach CMA law. It is necessary to teach the CMA law because it is a very specialised law. In order to develop the regulations to apply judgement-led approach the CMA's staff must be able to use their discretion power correctly.

Participant No. 2 stated:

Until now there is lack of sufficient implementation of the CML and its Executive Bylaws. According to the CML, the CMA must establish an academic institution to teach CMA law but until now this institution has not been established. There is no university in Kuwait which teaches CMA law and its bylaws. So in order to apply a developed approach like risk-based and judgement-led approaches, the CMA must change their strategy to improve education channels.

Participant No. 3 stated:

There is no course in Kuwait University to teach financial law because unfortunately there is no qualified teacher to teach this subject and no textbooks about CMA law. So to be honest if the CMA wants to appoint qualified staff, they must establish their own institution to teach financial law and adopt judgement-led approach.

Participant No. 4 stated:

There is no module in Kuwait University that teaches the CMA law. There is however a proposal to teach the topic after two years in postgraduate studies. However, the CMA staff need to be trained on regular basis to update their information and to adopt new policies such as risk-based and judgement-led approaches. There is no mandatory course for the CMA staff to take during their work at the CMA. This will affect the quality of the CMA staff.

Participant No. 5 stated:

We can say that the financial law is new to the industry, which needs time and great efforts to improve the current training and educational system. We can't blame the CMA staff for not having the qualification to understand and improve risk-based and judgement-led approaches, but we can say that we are looking at changing this.

Participant No. 6 stated:

There are no qualified staff in the CMA to implement a judgement-led approach. Even the CMA's workshops are not useful. Some of them are insufficient and do not provide enough information to the audience. One of the practical problems is that the speaker is specialised in a very specific area and cannot answer all questions. The CMA staff must have training programmes to understand the CML and its implications.

### 6.2.3 Data challenges

Gathering information and analysing data are the most significant tasks that regulators face. It is important that the regulators have a disclosure regime which helps to uncover risk and exercise judgement. Any judgement needs information, and not just any information – it must be accurate, precise and clear. This system requires a clear framework to determine the responsibility of each actor.

In fact, there is sufficient data gathering in the CMA system, as Chapter 6 explains, but no clear mechanism to analyse the data and draw the right conclusions.<sup>250</sup> For example, Kuwaiti listed companies disclose material information to stock markets, but the Boursa Kuwait Securities Company (Boursa)<sup>251</sup> and the CMA do not have a clear analysis mechanism to assess this information and set priorities accordingly.<sup>252</sup> It is impossible to adopt a judgement-led approach without a clear legal framework to analyse the market data.

### 6.2.4 Contestability of judgement

A regulator's knowledge of the market and how to make a judgement will be open to challenge. There is doubt about the ability of the Kuwaiti financial regulator to use its resources to reach the right judgements about risks or markets. It requires huge confidence in the regulator's legal system and how the system works in terms of the ability to hold the regulator accountable. There are processes and stages to reach a judgement, including interpretation of risks that affect the firm's risk profile, and this might lead to disagreements between the regulator's staff and regulated firms.<sup>253</sup> Therefore these decisions must be based on experience and proper knowledge of risk in the financial sector. The wrong decision can lead to a lack of trust in the regulator's ability to supervise and enforce the law, or even to protect the market by issuing the efficient regulations.

To adopt a judgement-led approach, the CMA is required to provide fit and proper evidence of its ability to make an accurate judgement, and the CMA might not be able to provide this due

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<sup>250</sup> Hussain Boarki, 'The legal protection for Capital Market Authority' Case study Kuwait and France, above (n 4) 340; see also Mohamad AlMutairi, above, (n 24) 602

<sup>251</sup> Boursa is the responsible authority to manage the material and intellectual assets of Kuwait Stock Exchange and to undertake the administrative and financial duties required to manage the Exchange, the Board of Directors of the said company shall replace the Stock Exchange Committee.

<sup>252</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68), 700

<sup>253</sup> Joanna Gray and Christian Metzger Peter above, (n 236) 233.

to its lack of expertise. In UK this argument already made by Icelandic bank which challenges the FSA there is lack of proper evidence for any specific.<sup>254</sup>

In summary, the current situation in the CMA does not help to adopt new approach like judgement-based regulation. It provides too much discretionary power for the CMA to exercise judgement over firms and risk.

## **7. Conclusion**

It is not suggested that the example of the UK FCA conclusively proves that forward-looking and interventionist regulation is superior to its pre-crisis risk-based alternative. There is solid evidence, indicated by the scholarly views cited here, that a risk-based approach can be effective in supervising and enforcing regulation in the financial sector. In fact, there is no guarantee that any approach can protect the market from a financial crisis, but countries will continue to suggest and adopt more developed approaches to the problem. Kuwait must take advantage of such developments to avoid facing the same challenges that the UK regulator faced during the financial crisis in 2007–2008.

The different points developed in the previous sections can be summarised in two main conclusions. Firstly, there is little question that in response to the dramatic, and potentially irreversible, damage inflicted by the 2008 crisis on many global financial markets, the UK decision to create the FCA resulted in positive outcomes. The FCA's commitment to a forward-looking and far more interventionist regulatory approach, as defined above, has proven effective. The case law and academic commentaries, while not universal in their support for the FCA, do give a strong endorsement to the current regulatory efforts. There is legitimate optimism that the FCA is on the right track to continue to provide effective oversight of the markets that fairly balances public and private interests. The forward-looking approach has proven superior to the former risk-based philosophy in the UK experience.

Secondly, concerning the CMA approach to adopting best practices, Kuwaiti financial markets are not as well developed as those that have existed in the UK for many decades. Although the two national legislative instruments use different language, it is apparent that the CMA and its UK counterpart are tasked to achieve the same market objectives –

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<sup>254</sup> Ibid. 238.

objectives driven by the public interest.<sup>255</sup> A general observation is also prompted in this respect: the CMA is widely regarded as having contributed to an improved Kuwaiti approach to financial market regulation in the post-crisis era, and one that adheres reasonably closely to international practice.<sup>256</sup>

In the still-evolving CMA context, strict adherence to rigid market regulation rules is far more likely to create ‘gaps and inconsistencies’. Worse, a rigid rules framework is vulnerable to persons and firms engaging in ‘creative compliance’, where loopholes are found, requiring regulators to devise new rules that might be circumvented.<sup>257</sup> This will affect the application of a risk-based approach. On the other hand, the CMA is in the process of developing and improving the current structure to apply a risk-based approach to regulation; the above analysis highlights the shortcomings in the CMA which hinder adopting this approach. First, the CMA must issue public statements about the adoption of a risk-based approach, and work together with regulated firms to apply the approach correctly. Second, the risk framework should be outlined and explained to the CMA’s staff and regulated entities to ensure it is applied correctly. Thirdly, the CMA must be aware of the limitations of the risk-based approach in terms of its inability to calculate future risk and immeasurable risk. Those shortcomings must be recognised by the CMA to avoid the mistakes made by the UK FSA (now the FCA), which led to the Northern Rock collapse.

Furthermore, this analysis shows that a judgement-led approach cannot be applied in Kuwait due to deficiencies in the CMA strategy and structure. The absence of knowledge about the judgement-led approach in the CMA and the Kuwaiti financial industry is an obstacle to applying the approach; and the lack of a mechanism to analyse the data has a huge effect on a judgement-led approach, as it leads to bad judgements. Thus the current structure, tools and powers of the CMA are not adequate to adopt a judgement-led approach: there is a need for

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<sup>255</sup> Capital Markets Authority, ‘Regulation’ (2018) Available: <<https://www.cma.gov.kw/en/web/cma/cma-handbook>> accessed 30 December 2019

<sup>256</sup> Capital Markets Authority, ‘Regulation’ (2018) Available: <<https://www.cma.gov.kw/en/web/cma/cma-handbook>> accessed 23 January 2020; (ii) UK Government, ‘Overseas Business Risk – Kuwait’ (2017) Available: <<https://www.gov.uk/government/publications/overseas-business-risk-kuwait/overseas-business-risk>> accessed 13 March 2020.



further improvement in terms of knowledge of the approach among the CMA's staff and the industry.

## Chapter 3: Understanding the Origins of the Kuwait Financial Sector

### 1. Introduction

An effective supervisory regime is a precondition for stability in the financial sector,<sup>258</sup> and to achieve the research objectives it is important to understand Kuwait's regulatory model for supervising financial services and stock markets. This includes the mechanism and procedures to decide Kuwaiti policy and how the different supervisory authorities work to regulate the markets. The goal is to explain how the institutions for financial sector regulation are structured, because this is crucial and has a direct impact on the quality of regulatory supervision and financial development.<sup>259</sup> It is also important to evaluate how appropriate Kuwait's legal structure is for adopting a risk-based approach. Studies show there is no perfect or ideal regulatory model for securities markets:<sup>260</sup> each model is based on the political and economic framework, domestic laws and cultural context of the country in question.

This chapter explores the rationale and reasons for Kuwait's regulatory development and how its financial policies are shaped. It discusses the extent to which the IOSCO Principles for Cooperation in Regulation are being implemented in the Kuwaiti context. The first section illustrates Kuwaiti democratic oversight to understand the independence and accountability system. The second section covers the regulatory landscape of the financial sector, explaining the delay in regulating the sector and the eventual establishment of a supervisory authority to oversee financial markets. It also describes the legal challenges that were faced in developing the law. The third section explains the dynamics of the supervisory authority and how it works to oversee stock markets in terms of sharing information.

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<sup>258</sup> David Mayes, Liisa Halme and Aarno Liuksila, *Improving banking supervision* (Springer 2001) 65.

<sup>259</sup> Martin Melecky and Anca M Podpiera, 'Institutional structures of financial sector supervision, their drivers and historical benchmarks' (2013) *Journal of Financial Stability* 9.3 428-444, 429-430.

<sup>260</sup> David Llewellyn, 'Institutional structure of financial regulation and supervision: the basic issues' (2006). A paper presented at the WB Seminar, Washington DC. At: <<<http://siteresources.worldbank.org/INTTOPCONF6/Resources/20572921162909660809/F2FlemmingLlewellyn.pdf>>> accessed 13 March 2020, 2. see also Kenneth Kaoma Mwenda and Alex Fleming, 'International Developments in the Organizational Structure of Financial Services' (2001). A paper presented at a seminar hosted by the WB Financial Sector Vice-Presidency, Washington DC see also Raghda Al-Qatanani, 'Legal Regimes to Counter Insider Dealing and Market Abuse: A Comparative Analysis of the UK and Jordan' (PhD thesis, University of Newcastle, 2013) 24.

## 2. Democratic oversight in Kuwait

Democratic oversight is a system whereby a regulator is accountable to ministers or directly to parliament for exercising its regulatory functions.<sup>261</sup> It is important to clarify briefly how the separation of power works in Kuwait. Kuwait's constitutional law and the CML are the main pieces of legislation framing the relationship between the CMA and the Council of Ministers. There are concerns that the Council of Ministers might have too much power over the CMA (discussed in Chapter 4). Their relationship is such that the CMA must have independence in relation to its decisions, but at the same time it is under the supervision of the Council of Ministers and is accountable to that body. Systemic risk can be found in the position of the CMA as an administrative regulator, since independence usually comes at the cost of limited accountability.<sup>262</sup> As a public body, the CMA must be linked to the Council of Ministers pursuant to the constitutional principle which confirms that any public authority must be subject to the control and supervision of the Council of Ministers.<sup>263</sup> Most Kuwaiti public services and utilities are owned by the government and the system uses the classical forms of democratic oversight: basically, public bodies are subject to direction by and accountable to the responsible minister and through them to parliament.<sup>264</sup> It seems that Kuwait still adopts the classical form of democracy, with all the deficiencies in this system. State ownership of public industries has been critiqued, because in practice the state exercises its power in favour of producers rather than consumers.<sup>265</sup> It is highly desirable for the Kuwaiti legal system to reconsider the definition of and legal framework for democratic oversight. Furthermore, it is noticeable that the Kuwaiti disciplinary system is associated with command-and-control regulations. It is a system where regulations are backed by a deterrence approach to ensure

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<sup>261</sup> Dawn Oliver, 'Regulation, Democracy, and Democratic Oversight in the UK' in Dawn Oliver & Tony Prosser, 'The Regulatory State: Constitutional Implications' (Oxford University Press, 2010) 243.

<sup>262</sup> Yousry Al-Assar, 'The legal system of the Capital Markets Authority and its effectiveness in achieving its objectives: case studies of Egypt, France and Kuwait' (2016) 4 (15) Kuwait International Law School Journal 38., see also Asim Jusic, Farah Yassen, above, (n 30) 55-60.

<sup>263</sup> Kuwait Constitution, Article 123.

<sup>264</sup> Dawn Oliver, above (n 261) 243 247. See also World Bank Group report available at << <https://siteresources.worldbank.org/PUBLICSECTORANDGOVERNANCE/Resources/AccountabilityGovernance.pdf>>> accessed 13 March 2020.

<sup>265</sup> Julia Black, 'Talking About Regulation', (Public Law, 1998) 77105 cited in Dawn Oliver, 'Regulation, Democracy, and Democratic Oversight in the UK' in Dawn Oliver & Tony Prosser, 'The Regulatory State: Constitutional Implications' (Oxford University Press, 2010) 248.

compliance. There are limitations and drawbacks to using command-and-control regulations as the method for regulating the financial sector.<sup>266</sup>

### **3. The new regulatory landscape**

After the 2008 financial crisis Kuwait reformed its regulatory structure to improve the financial sector. There are basically three regulatory authorities in the Kuwaiti financial system: the CBK, the MOCI and the CMA. They are responsible for regulation and supervision of the banking and non-banking sectors. The success of the new regulatory framework depends on effective coordination between these authorities,<sup>267</sup> thus it is important to provide the tools and mechanisms to ensure coordination in supervising and enforcing financial regulation.

The CBK is responsible for supervising all local banks and local branches of foreign banks, investment companies that are engaged in finance activities and exchange companies.<sup>268</sup> It may be noted that prior to the adoption of the CML, investment companies and investment funds were solely under the supervision of the CBK.<sup>269</sup> The CMA, established by the CML and the focus in this research, is now responsible for supervising and overseeing investment companies and investment funds. Kuwait's domestic banks, all of which are listed on the local Kuwait Stock Exchange (KSE), fall under the supervision of the CMA regarding their securities activities. Currently, there are 175 listed companies in the KSE.<sup>270</sup> Finally, insurance companies fall under the MOCI, which is responsible for establishing, licensing and supervising such companies. This clear legal framework for supervision complies with the IOSCO Principles, which aim to define the supervisory authorities in clear framework. The activities of the CBK and MOCI are not the focus of this research, which explores these authorities only in relation to the CMA's remit to supervise and enforce law in the financial sector.

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<sup>266</sup> Anthony Ogus, 'Regulation: Legal Form and Economic Theory', (Oxford, 1994), see also Anthony Ogus, 'Comparing Regulatory System: Institutions, Processes and Legal Forms in Industrialised Countries' (2002) Working Paper Series no.35, Centre on Regulation and Competition, 22.

<sup>267</sup> Nikoletta Kallasidou, above, (n 249) 130.

<sup>268</sup> Ministerial Decision No 38 of 2011 published on 18 September 2011, Article 6.

<sup>269</sup> Ahmad Al-Kandari, *Commercial Banking & Financial Institution, Kuwait* (Al-Falah Books 2009) 15.

<sup>270</sup> Kuwait Stock Market (Boursa Kuwait) <<<https://www.boursakuwait.com.kw/market-participants/listed-companies>>> accessed 13 March 2020.

The CMA is responsible for financial services, including licensing of intermediaries, fund managers, clearing agents and investment advisers.<sup>271</sup> In addition, Islamic investment companies that are practising securities activities in compliance with Shari'a principles are under CMA supervision.<sup>272</sup> Some listed company like insurance companies are licensed by MOCI not CMA where there is no unified rule to issue licenses for those companies. It is important to set standards and unified rule to issue a license for insurance companies. The CMA is responsible for ensuring listed companies' and non-banking institutions' compliance with the CML and its implementing regulations to ensure a secure, fair and orderly investment environment that enhances investor and public safeguards and promotes the proper regulation and development of the industry.<sup>273</sup>

Kuwait's financial sector comprises three levels of authorities. At the top are the Council of Ministers and the MOCI. At the central level, the CMA is responsible for regulating and enforcing financial rules according to the CML, which was issued by the National Assembly. It is also delegated by law to issue any Executive Bylaws needed to organise and enforce financial regulations. This delegation has the condition that a new provision cannot be contradictory to the CML. The third level is the self-regulating organisations involved in stock markets and exchanges, namely Boursa and the Kuwait Clearing Company (KCC). They are under the umbrella of the CMA, and need a licence from the CMA to operate in the stock markets.

All these supervisory authorities must work together in a cooperative and coordinated manner to ensure a strong financial system in Kuwait.<sup>274</sup> The CML allows cooperation with other regulators and agencies through memoranda of understanding (MoUs) to establish mechanisms and procedures to apply best practices in financial markets. Prominent experts and practitioners consider the CML to be the most significant law promulgated by the National Assembly, especially concerning its interpretation, application and enforcement.<sup>275</sup>

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<sup>271</sup> CML, Article 4.

<sup>272</sup> Kuwait legal system is civil law not all rules and regulation must be according to Shari'a principles.

<sup>273</sup> CML, Article 3.

<sup>274</sup> Nikoletta Kallasidou, above, (n 249)130. See also Eilis Ferran, above, (n 248) 14. See Ayman Al-Buloushi, 'Corporate Governance in Kuwait' (PhD thesis, University of Dundee 2013) 11.

<sup>275</sup> Abdullah AlKharafi and Abdullah AlHaroun above, ((n 38) 221. See also Abdullallah AlHayyan and Moahamad AlMuatari, above, (n 68) 55. See Adel AlManea, above, (n 9) 55.

The key problem associated with the multiple supervisory authorities approach to governing the banking and non-banking sectors is the level of communication and cooperation between the different authorities. Coordination and cooperation between the supervisory authorities is important for the stability of financial markets.<sup>276</sup> Coordination among authorities (which often have disparate interests and perspectives) can help to ensure that any laws passed will serve the interests of all supervisory authorities and prevent ill-considered laws from being passed or even considered.<sup>277</sup>

Sharing information between the authorities is the most important aspect of cooperation, and can be clarified in their MoUs.<sup>278</sup> The gaps between the laws and regulations as well as duplication between authorities can all be resolved through coordination and cooperation.<sup>279</sup> Coordination in supervising financial markets helps to improve the effectiveness of the oversight process.

This research concentrates on the domestic dimension in relation to the supervisory authorities in Kuwait. It focuses on coordination between the authorities in terms of sharing information about investment companies to assess their risk in stock markets. It is necessary to have an information-sharing system to improve cooperation between the regulators. As the Hampton Review recommends:<sup>280</sup>

over the longer-term regulators should look to improve cooperation and data sharing to reduce the need for businesses to submit the same data more than once; no proposal for significant upgrades or enhancements to existing regulators' IT systems should go ahead without prior scrutiny by the proposed Better Regulation Executive.

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<sup>276</sup> Mohammad AlMoqatei, 'Forms of Governance in the Kuwaiti Legal System', 2016) 4 (15) Kuwait International Law School Journal 35) 17-19.

<sup>277</sup> Chris Brummer, *Soft Law and the Global Financial System* (Cambridge University Press 2015) 25. OECD, 'OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators' (2014) available << <https://www.oecd.org/gov/regulatory-policy/the-governance-of-regulators-9789264209015-en.htm>>> accessed 13 March 2020.

<sup>278</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>> > accessed 13 March 2020.

<sup>279</sup> International Monetary Fund, 'Kuwait: Financial System Stability Assessment – Update', Report No. 10/239, July 2010) 24 available at << <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Financial-System-Stability-Assessment-Update-24096>>> accessed 13 March 2020.

<sup>280</sup> Philip Hampton, 'Reducing Administrative Burdens: Effective Inspection and Enforcement: Final Report' (March 2005) HM Treasury, London. 9.

The CML expressly allows cooperation with other authorities to organise the supervision process to cover all unregulated areas.<sup>281</sup> It empowers the CMA to establish links and relationships, and to cooperate with other markets and institutions, whether domestic or foreign, with a view to developing the markets. The CMA has signed two MoUs with the MOCI the first signed on 15 December 2014 and the second on 21 November 2017<sup>282</sup> to organise the legal framework regarding these four areas. Another MoU signed on 17 January 2018 between the CMA and CBK addressed the information-sharing process.<sup>283</sup> These MoUs help to increase the stability of the financial sector, in line with IOSCO standards. The most relevant principles pertaining to the regulators' work are IOSCO Principles 13–15, under category 'D', Principles for Cooperation in Regulation.

The MoU between the CMA and the CBK states that a regulator should send a letter to request information, addressed to a particular person in each supervisory authority who is responsible for receiving such requests and sending any information. There are weaknesses in the information-sharing process. First, a written letter is an inadequate way to gather information in an era when the world is becoming no more than a small village thanks to the internet and emails. Information must be shared quickly to protect market integrity. Second, there is no set period of time to respond to a CMA enquiry – for example, sometimes three days are given to reply to a request for information. The interviews revealed that 'it takes more than three days to obtain information from the CBK and in some other cases the CBK does not cooperate with us' (Participant No. 6). The rules need to set a time frame to answer any question or share information. There must also be an associated deterrence system to provide accountability for any delays or breach of the information-sharing concept. It is not practical to request other regulators to provide information and wait for three days when the information relates to commercial matters needing quick answers. Thirdly, there is no obligation for the CBK to provide the CMA with information. The obligation in the MoU outlines a general intention to exchange information without explaining the legal consequences to other entities.

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<sup>281</sup> Executive Bylaws, Module Two, Chapter two, Article 2.

<sup>282</sup> The CMA website available at <<https://www.cma.gov.kw/ar/web/cma/moui>> accessed 24 January 2020. Memoranda of Understanding between the CMA and the MOCI signed on 15 December 2014 and 21 November 2017 available at <https://www.cma.gov.kw/ar/web/cma/moui>, accessed 24 January 2020.

<sup>283</sup> Memorandum of Understanding between the CMA and the CBK signed on 17 January 2018 available <<https://www.cma.gov.kw/ar/web/cma/moui>> accessed 13 March 2020.

On other hand, in the MoU between the CMA and the MOCI concerning sharing information between the two authorities, the exchange of information is only discussed in section 4, the general rules, which states that in case of any violation of the CML and its executive law or the Companies Law, the CMA and the MOCI must exchange information to punish the non-compliant institutions. This section does not provide a full and proper framework for coordination regarding timing and reporting or informing. The absence of a sufficient legal framework may pose a hazard to the market. Hypothetically, if an institution were to breach a provision of the CML which led to significant damage to the market, and the MOCI had knowledge of this breach and did not inform the CMA immediately or there was delay in informing the CMA about the breach, how could the MOCI be held responsible for not informing the CMA or delaying in sharing information if the MoU does not determine any legal procedures for the two authorities to follow? Furthermore, in subsection 2 of section 4, regarding sanctions and punishment, the MoU states that the CMA and the MOCI should notify each other if any punishment or sanctions are applied to any institutions or employees. The specific details of the notification procedure must be improved to protect the markets from any negative impacts. For example, if a sanctioned institution is a major investor in the market it may affect the reputation of the market, hence the notification should include the reason for the punishment and it must be dealt with by both authorities in a confidential manner. These sorts of protections must be included in the MoU to achieve proper coordination between the authorities.

The coordination between authorities with respect to the MoUs is evidence of compliance with the IOSCO Principles, such as the need to ensure that procedures are clear and to avoid conflicts of interest, as set out in IOSCO Principle 8. However, some areas of improvement have been identified to ensure that cooperation and coordination are effective. It is suggested that a joint committee between the three authorities should be established to facilitate the exchange of information. A non-binding committee could follow up urgent matters such as investigating non-compliant institutions or sharing information. It also helps to ensure that interpretation of information is identical in the three authorities, because differences in their activities could lead to differences in interpretation. Creating a joint super-committee is a coordination and cooperation mechanism that would help to improve supervision and enforcement procedures in the financial sector.



To conclude, there is a clear need for more coordination in respect of sharing information between the supervisory authorities. The ultimate goal is for the financial markets to function with integrity, to create confidence in the domestic market and attract new investors. It is also important to apply the risk-based approach correctly. Each supervisory authority should set its priorities based on a risk assessment of the regulated firms, and allocate its resources to the firms that present the highest risk to its objectives. Sharing information is an important element to assess regulated firms' risk properly. Thus it is necessary to improve the current information-sharing process to apply the risk-based approach better.

#### **4. Regulatory framework of stock markets**

The CMA is responsible for regulatory policy, but it cannot do its job in isolation. The private sector needs to be more involved in the CMA's work to improve public–private cooperation. Regulatory governance addressing such cooperation should take into consideration self-regulation.<sup>284</sup> The merits of self-regulation have been subject to considerable debate. The Executive Bylaws issued by the CMA included provisions about self-regulation in the Kuwait legal system, which is line with the IOSCO standards. Boursa and the KCC are two institutions with fully self-regulating organisational status.<sup>285</sup> This use of self-regulation allows the Kuwaiti stock markets to gain maturity and experience.

The KCC and Boursa are the CMA's cornerstones for overseeing Kuwaiti stock markets. Coordination and sharing information between these authorities under the direction of the CMA are important in elevating the country to the level of an Emerging Market on global indices.<sup>286</sup> Recognising weaknesses in the system for sharing information between the CMA, Boursa and the KCC, the CMA procured new XBRL software to facilitate this.<sup>287</sup> The process of overcoming the weaknesses in sharing information is very slow. It took more than ten years to implement the XBRL software to exchange information between the authorities, and it is

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<sup>284</sup> OECD, 'The Need For Stronger Regulatory Governance', in *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest*, (OECD Publishing, 2011) 90 available at <http://dx.doi.org/10.1787/9789264116573-7-en>>> accessed 12 July 2020

<sup>285</sup> International Monetary Fund, 'Kuwait: Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism (Report No. 11/268, September 2011) available << <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Kuwait-Detailed-Assessment-Report-on-Anti-Money-Laundering-and-Combating-the-Financing-of-25210>>> accessed 13 March 2020.

<sup>286</sup> Jusic Asim and Yassen Farah, above (n 30) 50

<sup>287</sup> The CMA report for the financial year 2018/2019 available at <<https://www.cma.gov.kw/en/web/cma/annual-reports>> accessed 13 March 2020.

still not completely operational<sup>288</sup> (see Chapter 6 for more details). This software is designed to help avoid duplication and provide the same information for different authorities at the same time. A lack of adequate procedures for information exchange and coordination affects the risk assessment process used in applying a risk-based approach. The framework between supervisory entities must serve the ultimate goal of protecting the markets by assessing the highest risks and setting the CMA's priorities in overseeing listed companies. The following paragraphs explain the structure of the three authorities in stock markets and their role in supervising listed companies.

First, the privatisation of Boursa is an important step towards improving the government's financial and administrative position in the financial sector.<sup>289</sup> It aims to increase private share ownership to overcome the drawbacks in public management.<sup>290</sup> In February 2019 the first stage of the Boursa Kuwait Securities Company privatisation process was completed by the announcement of the winner in the bidding for a stake of 44 per cent, in accordance with CML Article 33. The stake was awarded to a consortium comprising Hellenic Exchanges-Athens Stock Exchange SA Holding, National Investments Company, First Investment Company and Arzan Financial Group.<sup>291</sup> The second stage, to sell a further 50 per cent of the shares to Kuwaiti citizens, was completed on 2 December 2019.<sup>292</sup> Upon the allocation of these shares, Boursa Kuwait will be 94 per cent owned by citizens and the private sector, while the Kuwaiti government, through the Public Institution for Social Security, owns the remaining 6 per cent. In essence, Boursa was established with the aim of taking over and managing the Kuwait stock market and progressively transitioning its operations while delivering on three main fronts: transparency, efficiency and accessibility. Its vision is to 'develop a liquid, reliable and sound capital market providing issuers with efficient access to capital, and investors with diverse return opportunities'.<sup>293</sup>

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<sup>288</sup> State Audit Bureau report for financial year 2017/2018 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>289</sup> Fahad AlZumai, 'An Assessment of Kuwaiti Privatization Law from Economic and Legal Perspective', (Journal of Law no.4 vol.37, 2013) 229.

<sup>290</sup> Ibid. 225.

<sup>291</sup> Kuwait newspapers, Available << <https://news.kuwaittimes.net/website/history-made-as-national-investment-company-consortium-takes-equity-stake-in-boursa-kuwait/>>> accessed 13 March 2020.

<sup>292</sup> The CMA website << <https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/detail/997927>>> accessed 13 March 2020.

<sup>293</sup> Boursa Kuwait, 'Vision and Mission' <<http://www.boursakuwait.com.kw/boursakuwait/page.aspx?page=43>> accessed 13 March 2020.

Furthermore, Boursa has been upgraded in status by the leading global indices. In September 2017 the Financial Times Stock Exchange upgraded Boursa from Frontier to Emerging Market status in its Russell Emerging Markets Index.<sup>294</sup> In December 2018 S&P Dow Jones Indices added Boursa to its Global Benchmark Indices with an Emerging Market classification effective prior to the market opening on 23 September 2019.<sup>295</sup> The most recent change was Boursa's upgrade to Emerging Market status by Morgan Stanley Capital International in November 2019, subject to two conditions<sup>296</sup> related to omnibus account structures and the same National Investor Number cross-trades being made available for international institutional investors before the end of November 2019. Kuwait implemented these conditions in October 2019, and Morgan Stanley announced that the 'it will reclassify the MSCI Kuwait Indexes to Emerging Markets status as part of the May 2020 Semi-Annual Index Review in one step as the Kuwait Equity Markets now meets all the necessary requirements'.<sup>297</sup> This is vital for the country's development, as it enables Kuwait to join the international market.<sup>298</sup> This achievement increased the need to improve the current financial regulation to attract new investors in the market. The CMA's strategy for adopting a risk-based approach must be clear, as poor regulation can damage the market and lose investor trust.

The KCC works under the umbrella of the CMA as a central clearing and settlement agency. The CMA has the power to grant clearing company licences for one or more clearing house activities.

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<sup>294</sup> The CMA, 'Boursa Kuwait is Upgraded from Frontier to Emerging Market Status' (Press Release dated 30 September 2017) available << <https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/detail/486000>>> accessed 13 March 2020.

<sup>295</sup> The S&P Dow Jones Indices, 'S&P Dow Jones Indices' 2018 Country Classification Consultation Results' (Index Announcement dated 5 December 2018) available << file:///C:/Users/u1664319/AppData/Local/Packages/Microsoft.MicrosoftEdge\_8wekyb3d8bbwe/TempState/Downloads/828959\_spdji2018countryclassificationconsultationresults12.5.2018%20(2).pdf >> accessed 13 March 2020. The CMA announcement << <https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/997927>>> accessed 13 March 2020.

<sup>296</sup> The CMA announcement, available at << [https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/view/searchResult?p\\_auth=1YDouMnD](https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/view/searchResult?p_auth=1YDouMnD)>> accessed 13 March 2020.

<sup>297</sup> The MSCI, 'MSCI to Reclassify the MSCI Kuwait Indexes to Emerging Markets' (December 2019) available at << [https://www.msci.com/documents/10199/238444/Kuwait\\_Press\\_Release.pdf/b78db0cf-33ca-feab-5594-0996870b6c19?t=1576706357233](https://www.msci.com/documents/10199/238444/Kuwait_Press_Release.pdf/b78db0cf-33ca-feab-5594-0996870b6c19?t=1576706357233)>> accessed 13 March 2020

<sup>298</sup> The CMA website available at <https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/486000>> accessed 13 March 2020.

## **5. Conclusion**

This chapter outlines the origins of Kuwait's democratic oversight system. It discusses the establishment of the CMA as a public authority, which is the legal basis of its public accountability, and how the public authorities work under the supervision of the government. It highlights the nature of the disciplinary system in Kuwait, which is associated with command-and-control regulations.

The chapter explains the structure of the financial supervision system by defining the responsibility of each supervisory authority in the financial sector and addressing the relationship between the CMA, the MOCI and the CBK. It also explains the CMA's coordination with the MOCI and the CBK to share information about financial services and stock markets. The analysis reveals that there is no mandatory obligation for the CBK and the MOCI to provide the CMA with information. The absent of a time frame for providing information is a weakness in Kuwait's supervisory system. There are major weaknesses in communication in sharing information, and these must be rectified to enable the CMA to adopt a risk-based approach. One suggestion is to establish a joint committee between the three authorities to exchange information through a proper and prompt channel.

There is another weakness in terms of the process for submitting information to the CMA and Boursa. Listed companies in stock markets are obliged to submit their disclosures to the CMA and Boursa separately, and there is no unifying mechanism to receive those submissions. The lack of proper procedures or a comprehensive system for submitting information leads to duplication. This weakness has been highlighted, but until now the CMA has not implemented the XBRL software to collect and analyse the data. Boursa, the KCC and the CMA work together to develop the stock markets and apply international standards, with the aim of organising Kuwait's financial sector so as to be able to adopt a risk-based approach and improve the current regulation. It is thus necessary to develop coordination between the three entities, and especially between the CMA and Boursa in relation to the disclosure process.

## Chapter 4: Architecture of Kuwait's Capital Markets Authority

### 1. Introduction

Strengthening the capital markets' governance structure is vital to achieving sustainable growth in market-based financing.<sup>299</sup> Accountability and an independent supervisory authority with appropriate powers and resources are fundamental to ensure the achievement of IOSCO's three core objectives of securities regulation: protecting investors; ensuring that markets are fair, efficient and transparent; and reducing systemic risk.<sup>300</sup> This chapter focuses on the CMA's formulation, capabilities and conditions, and the balance between regulatory powers. The CMA faces four key challenges in terms of its institutional nature and its position in the Kuwaiti financial sector. The first concerns the CMA's role in achieving its objectives. The second challenge relates to the CMA's position as an administrative regulator with limited independence. The third challenge concerns the balancing of power between the authority and the application of the accountability principle in the financial sector. The final challenge emerges from the application of international standards in the Kuwaiti legal system and the CMA's development in accordance with international governance principles. Each of these four distinct challenges is addressed in a separate section below.

To ensure effective governance structures the CMA has to manage, on a regular basis, the practical implementation of governance principles and standards.<sup>301</sup> It is often assumed that achieving effective regulation implies a need for strong regulatory enforcement.<sup>302</sup> It is important to note that while there is no formal governance structure dealing with effective supervision of global financial institutions, there are rules and regulations set forth by

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<sup>299</sup> OECD, 'The need for stronger regulatory governance', in *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest* (OECD Publishing, 2011) 74, available at <http://dx.doi.org/10.1787/9789264116573-7-en> accessed 23 February 2020.

<sup>300</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>> accessed 24 January 2020

<sup>301</sup> Asil Demirguc-Kunt, Erik Feyen and Ross Levine, 'Optimal Financial Structure and Development: The evolving importance of banks and markets (2011), 21 available at <<http://siteresources.worldbank.org/INTFR/Resources/DemirgucFeyenLevine060311.pdf>> accessed 24 January 2020.

<sup>302</sup> Bronwen Morgan and Karen Yeung, *An Introduction to Law and Regulation: Text and Materials*, (1<sup>st</sup> edn, Cambridge 2007) 153.

international organisations – which are considered as ‘soft law’ – to be followed in applying best practices.<sup>303</sup>

On 14 May 2017 the CMA chairman announced that the CMA attained official membership of IOSCO at its 42nd annual conference, 14–18 May 2017.<sup>304</sup> IOSCO has developed 38 Principles of Securities Regulation which need to be practically implemented within the Kuwaiti legal framework to achieve IOSCO’s objectives.<sup>305</sup> The 38 IOSCO Principles are grouped into nine categories, each of which has specific importance in developing the supervisory capacity of the Kuwaiti legal system.<sup>306</sup> The connection between investor protection and strong securities markets is important for economic growth.<sup>307</sup>

A risk-based approach to regulation requires the financial regulator to adopt clear objectives and assess each risk according to its impact on the achievement of those objectives,<sup>308</sup> thus it is important to ensure the CMA has clear objectives so as to implement a risk-based approach correctly. In addition, to achieve its objectives the regulator must be strong, independent and able to use all its resources without political influence to serve the public interest. But this independence must be associated with accountability to ensure that the regulator is using its powers and tools to achieve the regulatory objectives.

This chapter examines the CMA’s establishment and legal framework. It focuses on the independence and accountability of the CMA, and the balancing of power between the authorities. Finally, it deals with the CMA’s relationship with other authorities.

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<sup>303</sup> Emiliós Avgouleas, ‘Effective Governance of Global Financial Market: an Evolutionary Plan for Reform’ (2013) 4 (1) Global Policy 77 <[http://www.research.ed.ac.uk/portal/files/13204289/AVGOULEAS\\_E\\_Effective\\_Governance\\_of\\_Global\\_Financial\\_Markets\\_An\\_Evolutionary\\_Plan\\_for\\_Reform.pdf](http://www.research.ed.ac.uk/portal/files/13204289/AVGOULEAS_E_Effective_Governance_of_Global_Financial_Markets_An_Evolutionary_Plan_for_Reform.pdf)> accessed 13 March 2020.

<sup>304</sup> The Chairman of the CMA announced in 2016 that the CMA would become a member of IOSCO in the next conference. The most recent meeting of IOSCO was held in Jamaica in May 2017. The CMA announced on 14 May 2017 that the CMA had officially become a member of IOSCO: CMA Press Release, 14 May 2017 <<https://www.cma.gov.kw/en/web/cma/cma-board-releases/-/cmaboardreleases/detail/474086>> accessed 13 March 2020.

<sup>305</sup> IOSCO, ‘Objectives and Principles of Securities Regulation’, June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 13 March 2020.

<sup>306</sup> *ibid.*

<sup>307</sup> Bernard Black, ‘The Legal and Institutional Preconditions for Strong Securities Markets’ (2001) 48 UCLA Law Review 781, 785 and Part IV.

<sup>308</sup> Bridget Hutter, ‘The Attractions of Risk-Based Regulation: Accounting for the Emergence of Risk Idea in Regulation’ (200) 33 Centre for Analysis of Risk and Regulation Discussion Paper, 7.

## 2. Human capital

Adequately skilled human resources are crucial to applying a risk-based approach to regulation, because success depends on the staff's capacity to assess risk and evaluate it in order to set the CMA's priorities. The first issue concerning CMA staff is whether they are subject to the Civil Service Commission (CSC),<sup>309</sup> which is the public department responsible for all government employees in terms of salaries and promotion, or are part of the private sector, meaning the CMA can set salaries to attract more skilled staff. The CMA created its own administrative system to avoid attaching its staff to CSC rules and regulations, especially regarding salaries.

There is a connection between the CMA staff and the CSC in terms of required conditions set by the CSC for appointing any employee in a public body or ministry. It also sets rules and regulations for any contract that any public entity intends to enter into with foreign or domestic experts. According to CML Article 17, the CMA has full authority to set the administrative and financial bylaws for its employees' affairs, which negates the need to abide by the provisions set for civilian employees in CSC law. If there are no provisions in the CMA policies or systems, CSC law shall be applied. The chair of the Board of Commissioners has the powers of the minister and the CSC over what pertains to employees of the CMA.

This article gives the CMA full power regarding the appointment of its employees and determining its financial bylaws, but the CMA must submit a proposal to the CSC for its approval of the salaries and remuneration of CMA employees.<sup>310</sup> To improve the quality of its staff, the CMA can avoid using civil service pay scales and determine its own staff salaries and allowances. This gives the CMA full authority to appoint qualified and skilled staff.

Regarding the issue of whether CMA staff are public or private employees, or whether they are a unique category, the Kuwait Supreme Court in a judgment issued on 8 March 1993 said that 'any employee who works in a public body and who provides a public service should be considered as a public employee, even if this public body has their own laws and

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<sup>309</sup> The CSC was established on 1 July 1979 pursuant to Law No 15 of 1979.

<sup>310</sup> Civil Service Commission Law, Article 38, unofficial translation <<http://www.ilo.org/dyn/natlex/docs/SERIAL/39896/71907/F1019404829/KWT39896.pdf>> accessed 13 March 2020.

regulations'.<sup>311</sup> Thus CMA employees are public employees, and all public employees' rights and protections shall be applied. In this context, if there is a dispute regarding promotion, remuneration or termination, CMA employees can file a case in the administrative division courts. This discussion is important in determining the obligation of CMA staff to comply with the CSC Code of Conduct and any other rules, and identifying their liability to comply with regulations. The CMA has full independence and freedom to make staffing decisions in terms of administrative matters; the CSC becomes involved only if there is no provision within the CML to deal with the situation. This gives a clear framework for CMA staff responsibilities in complying with CMA rules and decisions regarding their work at the CMA.

Staff professionalism is an important element in successful application of a risk-based approach. Although the CML gives the CMA full independence to appoint skilled staff, there is a belief that the CMA only appoints staff who are part of a lobby of elite political and market players. As Participant No. 6 clarified, appointment and promotion in the CMA are subject to political influence. CMA staff got their jobs through *wasta*<sup>312</sup> without having the required qualifications and skills. *Wasta* is kind of corruption which facilitates the appointment and promotion of unqualified staff in public services.<sup>313</sup> It is a disease in the Kuwaiti system that destroys opportunities to appoint skilled staff in different public authorities. The CMA is no exception. Several reports by public authorities have highlighted the unfair practice of appointing staff without following legal procedures.<sup>314</sup> The CMA tried to overcome this criticism by obliging any new candidate to pass all the required exams and interviews.<sup>315</sup> Those procedures help to improve the quality of the CMA's staff, but there is still the belief that *wasta* has an impact on CMA staffing decisions at interview stage: a

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<sup>311</sup> Kuwait Supreme Court, Case No 56 of 1992, Commercial Division, 8 March 1993.

<sup>312</sup> Often Arabs referred to it as Vitamin W, which is the magical word that smoothes the way to jobs, promotions, university places and much else besides. See al-bab newspaper available at << <https://al-bab.com/society-politics/wasta>>> accessed 13 March 2020. 427- 4

<sup>313</sup> Abrar Al-Ezni, 'The Influence of Wasta on Knowledge Sharing in Kuwait' (2017) Proceedings of the 18th European Conference on Knowledge Management 23, 25.

<sup>314</sup> State Audit Bureau report for financial year 2017/2018 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>315</sup> The CMA, 'Announcements of Vacancies' (13 January 2020) available <<<https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/1000981>>> accessed 18 March 2020.



candidate with a similar political alignment to that of the interviewer will get a high score and pass the interview, while other candidates will get a lower score due to political preferences.

There are staff shortages in the CMA trading department, but the CMA taken no action to cover this by appointing qualified staff.<sup>316</sup> CMA staff are often inexperienced and unskilled.

Another important element that indicates unqualified staff is the lack of effective training and awareness programmes to improve CMA staff.<sup>317</sup> Very few CMA personnel have undertaken training courses over recent years, hinting at the unfairness of procedures to appoint and train CMA staff. A State Audit Bureau report stated:<sup>318</sup>

92.4% of the CMA staffs have not taken any internal training courses over the last year, while 49% have not taken any external training courses.

The lack of qualified staff and adequate training in the CMA has a significant impact on the application of a risk-based approach. This needs immediate attention to change the CMA strategy to recruit and train staff. In addition, the latest development, the judgement-led approach, requires a regulator's staff to apply experience and knowledge in understanding a regulated firm's business and use their judgement to assess the firm's risk.<sup>319</sup> The ability to analyse and judge each and every vulnerability within a regulated firm depends on the expertise of the regulator's staff.<sup>320</sup> This definitely needs qualified staff with the required skill to use their judgement to achieve the regulatory objectives. Currently, the CMA staff lack training and skills to the extent that they cannot apply a judgement-led approach at all.

The Kuwaiti regulatory framework may be contrasted with the UK's system, wherein the FCA is incorporated as a private company but is accountable to parliament and subject to judicial review. The statute that created the FCA emphasises the independence of the

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<sup>316</sup> State Audit Bureau report for financial year 2017/2018, 431, 462 - 463, and 467,8 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>317</sup> State Audit Bureau report for financial year 2017/2018, 431, 462 - 463, and 467,8 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>318</sup> State Audit Bureau report for financial year 2017/2018, 462 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 13 March 2020.

<sup>319</sup> Eilis Ferran, 'The Reorganisation of Financial Services Supervision in the UK: An Interim Progress Report', above, (n 248) 12-13.

<sup>320</sup> Nikoletta Kallasidou, above, (n 249) 129.

authority, and provides adequate powers for it to exercise its policy without any influence or interference from government.<sup>321</sup>

### 3. Regulatory objectives

The CMA has several objectives.<sup>322</sup> It aims, *inter alia*, to regulate securities activities in a fair, transparent and efficient manner; to grow the capital markets, and diversify and develop investment instruments thereof in accordance with best international practice; to enhance investor protection; to reduce systemic risks arising from securities activities; to impose requirements of full disclosure to achieve fairness and transparency, and prevent conflicts of interests and the use of insider information; to ensure compliance with regulations related to securities activities; and to enhance public awareness of securities activities and the benefits, risks and obligations arising from investments in securities, and encourage their development. These seven objectives consist of general rules and principles that the CMA should follow; they are related to general objectives that all financial regulators should consider and which IOSCO has adopted. The CMA strategy of adopting objectives that comply with international standards is a very important step for globalisation and harmonisation of regulation, because it shows that international sources of foreign investment are increasingly looking for a common set of standards and behaviour.<sup>323</sup> Implementation of these common standards will help Kuwait's financial markets to grow and attract foreign investors.

In theory and on paper the CMA has adopted clear objectives, but in practice there are no enforcement mechanisms and no explanation of the purpose of the law.<sup>324</sup> In terms of the clarity of the objectives, Kuwait does comply with IOSCO standards, but the mechanisms to achieve these objectives do not exist. To achieve its objectives, the CMA must elaborate upon these rather general principles by translating them into rules. However, section 3 of the CML is merely a repeat of the previous section in the law,<sup>325</sup> and the law does not include any specifications or prescriptions. Thus there are many unanswered questions regarding the

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<sup>321</sup> Financial Services Act 2012 (UK)  
<[http://www.legislation.gov.uk/ukpga/2012/21/pdfs/ukpga\\_20120021\\_en.pdf](http://www.legislation.gov.uk/ukpga/2012/21/pdfs/ukpga_20120021_en.pdf)> accessed on 13 March 2020.

<sup>322</sup> CML, Article 3.

<sup>323</sup> OECD, 'The need for stronger regulatory governance', in *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest* (OECD Publishing, 2011) 74, available at <<http://dx.doi.org/10.1787/9789264116573-7-en>> accessed 24 January 2020.

<sup>324</sup> State Audit Bureau report for financial year 2017/2018 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 18 February 2020.

<sup>325</sup> Fatima AlShuraian, above, (n 4) 199.

application of these general objectives. For example, what kind of protection should the law consider? What does justice, equity or transparency mean? The interview data confirm this shortcoming in Kuwaiti financial regulations. There is no clarification regarding the purpose of the law or what it protects. There is a need to improve CMA regulations and rules to be clearer and more specific as to what each overall objective entails. As it is essential to apply a risk-based approach, the regulator's objectives must have clear and enforceable methods to assess the market risk.

The CMA posts its annual report on its website for the public to review. There is no mention of the regulatory policy in any of the CMA's reports or other documents,<sup>326</sup> and the strategy that the CMA applies is vague. The CMA stated in its annual report 2018/2019 that it had achieved its regulatory objectives, but there were no indicators to substantiate this claim.<sup>327</sup> It is worth mentioning that this report does not provide any concrete information: most of it is descriptive and repeats paragraphs from the CML and its Executive Bylaws. It is suggested that the CMA redesigns its reports and ensures that there is some underlying information about regulations and the policy on rules. It is also very important to clarify the policy and strategy that the CMA follows to enforce the CML. Another important note is that the CMA does not hold an annual public meeting (unlike the FCA, discussed below) for the public to discuss the report outcomes. It is contrary to the democratic concept not to allow people affected by the decisions or activities of a public body to participate in decision-making or to have access to information and suggest any necessary improvement to the laws and regulations.<sup>328</sup> The Kuwait system should give reasonable powers to market participants to get involved in decision-making.

In contrast, the UK approach is completely different. Part 2 of the Financial Services Act 2012 states very clearly that the FCA has three objectives: consumer protection, market integrity and competition.<sup>329</sup> These three general rules are further explained on the FCA website,<sup>330</sup> and each

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<sup>326</sup> The CMA website available at <https://www.cma.gov.kw/ar/web/cma/annual-reports> accessed on 13 March 2020.

<sup>327</sup> The CMA, '2018/2019 Annual Report' available at <<https://www.cma.gov.kw/ar/web/cma/annual-reports>> accessed on 11 February 2020.

<sup>328</sup> Dawn Oliver, 'Regulation, Democracy, and Democratic Oversight in the UK' in Dawn Oliver & Tony Prosser, 'The Regulatory State: Constitutional Implications' (Oxford University Press, 2010) 245.

<sup>329</sup> Financial Services Act 2012 –Part 1A Chapter 1- 1B.

<sup>330</sup> The Financial Conduct Authority, 'The FCA's Approach to Advancing its Objectives' (December 2015) <<<https://www.fca.org.uk/news/news-stories/fca's-approach-advancing-its-objectives>>> accessed 18 March 2020.

rule is defined in separate sections of the Financial Services Act 2012.<sup>331</sup> In addition, the FCA holds an annual public meeting to discuss its annual report,<sup>332</sup> allowing a public discussion about the outcomes and contents of the report. It is an opportunity for people to ask the FCA directly about the way it discharged or failed to discharge its functions, and this provides great transparency to the market.

The CMA's objectives and duties comply with IOSCO's Principles Relating to the Regulator. IOSCO Principle 1 notes that the responsibilities of the regulator should be clear and objectively stated. As mentioned, the responsibilities of the CMA – which is the designated regulator by law – are clearly defined, so in theory the regulatory objectives are clear but in practice the CMA needs more regulations to achieve these objectives.

The seven expert witnesses in this research all confirmed that the CML does not provide an explanation of the purpose of the law.

Participant No. 1 stated:

The CML itself does not explain its purpose but the explanatory memorandum of the law addresses the reason and the purpose of the issuance of the law. The CML is a complex law and has an economical dimension which makes it hard for the law drafter to indicate its purpose.

Participant No. 2 stated:

The explanatory memorandum should include more details about the purpose of the law and policy that the financial regulator must follow.

Participant No. 3 stated:

All the laws in Kuwait do not explain their purpose. Some laws are just a reaction to an event or a situation and the CML is an example of this.

Participant No. 4 stated:

The absence of the purpose of the law in the CML is a weakness in the law. It must state the purpose in order to apply it correctly and to protect investors and/or companies. It is also a means to hold the CMA responsible for achieving its goal.

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<sup>331</sup> Michael Blair QC, *Blackstone's Guide to the Financial Services and Markets Act 2000* (2nd ed., Oxford University Press 2009) 22.

<sup>332</sup> Financial Services Act 2012 SCHEDULE 3 IZA s.12.

As well as to hold it accountable in case of failure to achieve the goals and serving its purpose.

Participant No. 5 stated:

Maybe the CMA must focus to highlight the purpose of the law and issue a public statement in this regard.

Participant No. 6 stated:

We try to implement the law as written in the CML. I don't recall I needed to check the purpose of the law due to its absence.

Participant No. 7 stated:

While reviewing the cases, the judge finds difficulty when reviewing the law to discover the purpose of the law and what it should serve, to reach a fair verdict. There is no clear stated purpose of the law.

These statements clearly confirm that there is lack of clarification in terms of the purpose of the law and how to achieve the regulator's objectives. The risk-based approach needs clear stated objectives to enable the regulator to set its priorities and allocate its limited resources. This weakness must be addressed by a public statement from the CMA explaining and clarifying the purpose of the CML and setting indicators to analyse its application.

#### **4. Regulator independence**

It is important to define the terms 'independence' and 'accountability' before analysing whether they are appropriately applied within the Kuwaiti context, since both terms are connected.<sup>333</sup> IOSCO provides a clear definition of independence and accountability:

Independence and accountability are inter-related. Independence means the ability to undertake regulatory measures and to take and enforce decisions without external (political or commercial) interference. Accountability means that, in the use of its powers and resources, the regulator should be subject to appropriate scrutiny and review.<sup>334</sup>

Securing independence and accountability and facilitating implementation of the IOSCO Principles depend upon a number of factors, including an appropriate and effective legal

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<sup>333</sup> Eva Hüpkens, Marc Quintyn and Michael Taylor, above, (n 16Error! Bookmark not defined.) 2-3.

<sup>334</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' (May 2017) <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>>> accessed 18 March 2020.

setting, a supervision system, an efficient court system and an accounting framework within which the securities markets can operate.<sup>335</sup>

Independence is an important factor in achieving a sound regulatory authority able to oversee the financial sector. Theoretically, the Council of Ministers has only limited power over the CMA; but although the CML states that the CMA is independent, this does not mean that it is in practice. Accordingly, the next subsections analyse the reality of CMA independence in terms of its constitution, financial resources and reporting process.

The legal basis of the CMA's *independence* is Article 133 of the Kuwait Constitution, which grants the National Assembly the power to regulate public entities in such a way as to ensure their independence under the direct supervision of the government.<sup>336</sup> This article contains a constitutional principle stating that to protect people's rights, any matters related to commercial freedom, investment, property rights and competition must be regulated through a law issued by the National Assembly. Secondly, its *legal personality* means that the CMA is a legal person and has its own legal rights and obligations in relation to other entities, including the Council of Ministers and the courts. The inclusion of this principle in the CML helps to develop the CMA's independence and gives it legal protection so the CMA may act as a public body with domestic and foreign authority. Thirdly, the CMA is subject to the *oversight* of the Minister of Commerce and Industry, whose supervision impacts on the extent and parameters of both the CMA's independence and its accountability, as discussed in the next subsections.

#### 4.1 Constitution of the governing body (appointment, remuneration, term duration and vacancies)

The most important step in organising oversight of the financial markets is the establishment of the supervisory authority, which in Kuwait is the CMA. This ought to be done in compliance with IOSCO standards. According to CML Article 6, the CMA will be managed by the Board of Commissioners of the Authority, consisting of five full-time commissioners who should be appointed by decree upon nomination by the Minister of Commerce and Industry. The decree

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<sup>335</sup> OECD, 'Designing independent and accountable regulatory authorities for high quality regulation' Proceedings of an Expert Meeting in London, United Kingdom, January 2005, 33 <<  
<http://www.oecd.org/regreform/regulatory-policy/35028836.pdf>>> accessed 18 March 2020. See also Asim Jusic and Farah Yaseen, above (n 30) 30

<sup>336</sup> Article 133 of the Kuwait Constitution 1962, reinstated in 1992, English translation utilized here is from the Constitute Project.org <[https://www.constituteproject.org/constitution/Kuwait\\_1992.pdf?lang=en](https://www.constituteproject.org/constitution/Kuwait_1992.pdf?lang=en)> accessed on 18 March 2020.

shall also designate, from among the Board members, the chairperson and deputy chair. The Board is pre-eminent within the CMA and is responsible for all the CMA's decisions.<sup>337</sup> It is a concern that the CML did not grant actual independence to the CMA. Although the CML states that the Board of Commissioners shall have full autonomy in the management of the authority, the commissioners are appointed by decree after nomination by the MOCI.<sup>338</sup> The nomination of the commissioners and their affiliation to the MOCI undoubtedly affects their independence. Thus it is noted that the CMA does not reflect the principle of independence. The MOCI nominates candidates for the Board of Commissioners to the Council of Ministers, which issues a decree for the appointments.<sup>339</sup> This nomination process take place without consulting the appointed Board; even the private sector does not contribute, nor is it requested to nominate a candidate which would ensure that the commissioners are experts in their field. In most cases the minister will nominate a candidate who is a member of or allied with his political bloc;<sup>340</sup> this is confirmed by the interviews (see below). Furthermore, there is no distinction between executive and non-executive members in the CMA. As a result, political risk will necessarily exist in this scenario. It is recommended that the appointment of the CMA Board of Commissioners should be through election. Another solution could be to make the minister's proposals subject to certain conditions or requirements. For example, the minister should not be permitted to propose names of people who share the same political affiliation more than once, and the minister must consult with the private sector or previous commissioners to nominate commissioners to the Council of Ministers.

The interviews confirm that the procedures for the Minister of Commerce and Industry to nominate commissioners for the CMA Board are inadequate, which affects the CMA's independence.

Participant No. 1 stated:

We can say that the appointment of the CMA Board of Commissioners is completely in the government's hand. The minister proposes nominated names and the Council of Ministers discusses those names and approves or removes those nominations. To be honest, current Board of Commissioners are all experts in financial field. Even if the minister has to choose from a particular political party,

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<sup>337</sup> Executive Bylaws, Module 2, Chapter 4, Article 4.1.

<sup>338</sup> Nagham Al Dabbous, 'Corporate Governance Transformation: The Case of Kuwait' (PhD thesis, University of Aberdeen 2012) 112.

<sup>339</sup> Asim Jusic and Farah Yaseen, above (n 30) 45.

<sup>340</sup> In Kuwait, there is no law organizes the political parties, therefore its considered as political bloc.

he nominates qualified names to be Commissioner. We, on the other hand, have witnessed that one of the nominations has been removed during the Council of Ministers meeting based on political preferences and biases.

Participant No. 2 stated:

In terms of the appointment of the CMA commissioners, there is no authority responsible to review the nominations' CV and background check in Kuwait in any public position. The minister suggests the commissioners' names to the government to approve it and of course there is political influence in the appointing process. In fact the Minister always nominates commissioners who have experience in financial sectors. There are five commissioners: one of them must have a legal background and three from the private sector and the last one has Shia (Sheaa) background.<sup>341</sup>

All public service positions are appointed based on political preferences, but the CMA is a unique entity because it is constructed of five commissioners to limit the political influence on the board decision. It is difficult for the political bloc to have influence on five commissioners, to issue a certain decision about a company or markets. It is a mechanism to limit political influence on the CMA's decisions on daily basis.

Participant No. 3 stated:

Of course, the appointment of the CMA Board of Commissioners has political influence. This is the reality of the country: political influence appears in every sector.

Participant No. 4 stated:

It depends on the minister's political preference to appoint the CMA Board of Commissioners.

Participant No. 5 stated:

In terms of the appointment of the commissioners of the CMA Board, it is based on the minister's discretion to nominate a commissioner under political pressure. I think the minister himself should answer your questions if there is really political influence on his decision to appoint commissioner in the current board.

Participant No. 6 stated:

It is not just the appointment of the CMA Board of Commissioners under political influence, even promotion and recruitment in the CMA will be based on political preference.

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<sup>341</sup> Shia is one of the two main branches of Islam. They represent political lobby to protect Shia rights and interest.



The interviews also revealed another issue related to ministerial and National Assembly power to change the CMA structure to ensure their influence in CMA decisions. The current structure of five commissioners provides a balance to limit ministerial and political party influence on the CMA's decisions on a daily basis. As Participant No. 2 highlighted above, the existence of five commissioners is a way to limit political influence. In other words, it takes a lot to convince five commissioners to issue a certain decision, and the diversity of the commissioners makes this mission harder. Although the existence of five commissioners does not ensure the limitation of political influence if all these commissioners are from same political bloc, it can be risky if all the commissioners vote against the wishes of the government or National Assembly. The government or National Assembly will simply use another procedure to ensure their influence on the CMA Board by changing the structure of the Board, as noted by the interviewees.

Participant No. 2 said:

Some of the powerful groups who have private interests to influence the CMA's decision started a campaign to change the structure of the CMA Board to be one of the following scenarios.

- a) The Minister of Commerce and Industry to be the chairman of the CMA Board so they can influence the minister's decision easily. Like what happened to the National Fund for Small and Medium Enterprise Development: converted from being a technical institution to a political institution.
- b) A structure which is similar to Kuwait Central Bank to have only a governor and his deputy to make the influence much easier than five commissioners. The idea is to centralise the power on one person in order to change and influence his decision through the National Assembly or private sectors.
- c) A third scenario is to have five commissioners but only the chairman and his deputy to have a full-time job. The other three commissioners are part-timers.

When the powerful groups feel that the CMA's decisions are damaging their interest, they will use their power to change the CMA structure to achieve their goals and interest.

Participant No. 5 clarified that:

Currently, there are no intentions or discussions in the National Assembly to amend the structure of the CMA Board, in terms of their number or structure. There was a proposal to appoint only an executive manager to the CMA but this proposal has been rejected by the CMA Board. There was a precedent that the government was not happy with the chairman of the CMA, so the government changed the law to decrease the Board duration from five years to four years, therefore I will not be surprised if the structure of the CMA Board will be under political abuse.

The interviews reveal a new tool to punish the CMA commissioners: the Minister of Commerce and Industry and political parties will change the CMA Board when it issues an unpopular decision that affects the private interests of political parties. Changing the structure of the CMA Board does not aim to serve the public interest, but rather to serve the private interest of certain groups that are unhappy with the CMA decisions. The minister or the political party proposes an amendment to the National Assembly to change the structure of the CMA board from five members to one director. This takes away all authority from the commissioners hands and allows political influence on the director's decisions. The debate to change the structure of the CMA Board raised when the CMA referred the CBK governor to prosecutor. Further details about the referral in the following sections. It means this proposal is a reaction to those vents.

The interviews and the proposal to change the CMA structure show clearly how the CMA is under political influence and does not have sufficient independence from government. It is contended that the CMA does not comply with best practices regarding the appointment of the Board of Commissioners; in particular, it does not comply with IOSCO Principle 2, stating that the regulator should be 'operationally independent and accountable in the exercise of its functions and powers'.<sup>342</sup> Hence the CML needs to be amended so that procedures are adopted which will avoid, or at least minimise, the systemic risk that exists in the current procedures.

In terms of conditions for appointment to the CMA Board of Commissioners, under the CML potential commissioners must meet certain criteria: the candidate must be a Kuwaiti natural individual with integrity, and have experience or be specialised in fields related to the functions of the CMA.<sup>343</sup> Furthermore, the candidate must not have been the subject of a final judgment of bankruptcy, nor penalised with restriction of freedom for a felony or a crime of breach of honour or trust.<sup>344</sup> The conditions for the appointment of commissioners partially comply with the IOSCO Principles with respect to the specialisation required of regulators. To apply the highest professional standards it is necessary to appoint an expert, thus when the CML requires commissioners to have experience or be specialised in fields related to the functions of the CMA, it emphasises the application of the highest professional standards.<sup>345</sup>

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<sup>342</sup> Principle 2 of the IOSCO Objectives and Principles states that: 'The Regulator should be operationally independent and accountable in the exercise of its functions and powers.'

<sup>343</sup> CML, Article 7.

<sup>344</sup> Ibid.

<sup>345</sup> IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 18 March 2020.

These conditions and rules are important to apply best practices in financial services and stock markets. There are three critical elements for institutional independence: first, creating a clear legal framework that regulates the appointment and dismissal of commissioners and provides them with proper security of tenure; second, the commissioners must be experts; and third, the decision-making process must be transparent to the extent that this is consistent with commercial confidentiality.<sup>346</sup> The expertise in the Board of the Commissioners is essential to improving and developing the financial markets.

A major difference between the FCA and the CMA is that the FCA is a private company limited by guarantee.<sup>347</sup> It is an independent public body funded entirely by fees from the firms that it regulates. As Company No. 1920623, the FCA must comply with the Companies Act 2006. The Financial Services Act 2012 gives the FCA the power to organise and supervise firms and markets, which are subject to administrative public law. Another difference between the FCA and the CMA is the constitution of the governing body. The FCA process for selecting its governing body involves three parties, namely the Treasury, the BoE and the Secretary of State.<sup>348</sup> The chair, chief executive and at least one other member are appointed by the Treasury. The BoE deputy governor for prudential regulation is a non-executive member; two non-executive members are appointed jointly by the Secretary of State and the Secretary to the Treasury; and the majority of the governing body should be non-executive members.<sup>349</sup> The FCA procedures to appoint its governing body provide diversity and ensure that no political party can influence the constitutional process. But the most fundamental difference between the two systems is that the FCA appointments are subject to a governance code which came into effect on 1 January 2017.<sup>350</sup> This code ensures that FCA appointments are in accordance with government principles for public appointments. The governance code is a good solution to ensure that the appointment of the governing body is carried out without political influence.

Finally, the factor with the greatest effect on the independence of the governing body is the remuneration of commissioners. In the UK, the FCA governing body is appointed by several

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<sup>346</sup> Ibid.

<sup>347</sup> Edward J Swan and John Virgo *Market Abuse Regulation* (2<sup>nd</sup> ed, Oxford University Press 2010) 120.

<sup>348</sup> Financial Services Act 2012 SCHEDULE IZA available at <http://www.legislation.gov.uk/ukpga/2012/21/schedule/3/enacted> accessed on 24 January 2020

<sup>349</sup> Ibid.

<sup>350</sup> The Governance Code available at << <https://publicappointmentscommissioner.independent.gov.uk/regulating-appointments/governance-code/>>> accessed on 18 March 2020.

parties, as mentioned, and each party has its own rules and regulation to determine a commissioner's remuneration. In Kuwait the CMA Board's salaries are determined by a proposal by the Minister of Commerce and Industry and the consent of the Council of Ministers; a decree then sets the remuneration of the chair, the deputy chair and the rest of the commissioners, as well as any allowances or privileges paid from CMA funds.<sup>351</sup> It is clear that the CMA does not have full independence, and there is a conflict of interest. Four interrelated concerns arise with respect to the commissioners' salaries and remuneration.

First, regarding salary determination, the process in CML Article 11 may detrimentally affect the independence of the CMA because salaries are set by a proposal of the minister and a decision of the Council of Ministers, and no independent body is involved in the setting of the commissioners' remuneration. This is arguably a violation of IOSCO Principle 2, which states that the regulator 'should be operationally independent and accountable in the exercise of its functions and powers',<sup>352</sup> and Principle 3, which states that the regulator 'should have adequate powers, proper resources and the capacity to perform its functions and exercise its power'.<sup>353</sup>

Secondly, the oversight of salary levels affects accountability. The CMA is partly funded by the government and its budget is considered to be a public budget, thus the National Assembly should be able to review or have oversight of such an important area, especially if (as discussed below) the salaries are excessive.<sup>354</sup>

Thirdly, the salaries and remuneration decrees are not published, so there is a lack of transparency. There is no official record of the commissioners' salaries even in the CMA's annual report.<sup>355</sup> The decree which sets these salaries should be printed in the official government publication – the Kuwait Gazette, *Kuwait Al-Yaum* – where all legislation is

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<sup>351</sup> CML, Article 11.

<sup>352</sup> IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 24 January 2020

<sup>353</sup> *ibid.*

<sup>354</sup> The Commissioners' salaries are reported to be between 13,000 and 17,000 Kuwaiti Dinars per month, which is approximately 34,175 British Pounds. This was disclosed in a newspaper article in which the then-Minister of Commerce and Industry, Dr Amani Bouarsi, was reported to have asked the CMA Commissioners about their salaries: see AlAnba.com 21 September 2011 <<http://www.alanba.com.kw/ar/economy-news/228557/21-09-2011-الرد-دون-مبررات-بورسلي-تستفسر-رواتب-مفوضي-هيئة-الاسواق-والهيئة-تترفض>> accessed 24 January 2020.

<sup>355</sup> The CMA annual report available at <<https://www.cma.gov.kw/ar/web/cma/annual-reports>> accessed on 24 January 2020.

published. The UK approach differs: the FCA's annual report must include a statement of the remuneration of the appointed members of the FCA governing body for the year in question.<sup>356</sup>

This leads to the fourth and final concern: that the commissioners' salaries are excessive when compared to the average salaries of employees with similar university qualifications, and given the overall financial situation of Kuwait in the current constrained economy. Excessive salaries, which are set by the Council of Ministers but are obviously out of step with overall salary levels in the public sector – and which are kept secret – have the undesirable effect of reducing the appearance of the CMA's commissioners' impartiality and independence from the executive.

The term of service of the CMA's Board of Commissioners is clear in the CML. A commissioner's term of membership is four years, renewable for one term only, except for the first board members, of whom three can be renewed for a third term.<sup>357</sup> It is good practice that the law states the commissioners' term in office to ensure there is diversity in holding a position on the Board. Some public bodies have no limitation of the term of office, and an appointed member can hold a position for more than ten years.<sup>358</sup> It is one of the features of privatisation that helps to isolate the CMA from political influence by appointing the commissioners for a fixed term.<sup>359</sup> In the UK approach, the fixed term of service for the FCA governing body helps to increase open competition for public appointments.

#### 4.2 The CMA's budget

Funding is often a hidden problem. Sometimes the securities regulator has a minimal budget that prevents it from hiring qualified people, or the budget is so meagre that it fails to 'keep them honest'.<sup>360</sup> In other cases the budget may be affected by political and commercial influences which lead to obstacles in developing the markets.<sup>361</sup> Decent funding is essential for

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<sup>356</sup> Financial Services Act 2012 SCHEDULE IZA available at <<<http://www.legislation.gov.uk/ukpga/2012/21/schedule/3/>>> enacted accessed on 27 January 2020.

<sup>357</sup> CML, Article 10.

<sup>358</sup> The head of the Civil Service Commission hold his position for more than 25 years. It is not about good or bad practice but to ensure diversity in the financial sector is very important factor to develop the sector.

<sup>359</sup> Dawn Oliver, 'Regulation, Democracy, and Democratic Oversight in the UK' in Dawn Oliver & Tony Prosser, *The Regulatory State: Constitutional Implications* (Oxford University Press, 2010) 250.

<sup>360</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' above (n 12) 1577.

<sup>361</sup> Bernard S. Black, 'The Legal and Institutional Preconditions for Strong Securities Markets' above (n 307) 781-790.

strong securities markets. This subsection discusses the CMA's budget, financial resources and financial reserves.

First, there is a contradiction in the legislation between creating an image of CMA budgetary autonomy while simultaneously making it subservient to the Council of Ministers. The CML gives the CMA a large degree of independence in relation to the preparation of the budget, but at the same time it is linked to the Council of Ministers. In fact, prior to the 2015 amendments to the CML, the CMA budget did not need National Assembly approval and was completely under the CMA's power.<sup>362</sup> The interviews clarified that this situation was more appropriate to prevent political interference (Participant No. 1, see below). This situation of preparing and approving the CMA's budget without National Assembly approval is more likely to provide the CMA with independence.

The 2015 amendments to the CML regarding the CMA's budget were a result of political pressure to reform the CML in a manner that serves private interests.<sup>363</sup> According to Participant No. 4, the aim of these amendments was to ensure that the CMA's budget requires the approval of the National Assembly, thereby allowing indirect influence on the CMA's budgeting decisions. For example, MPs may withhold their approval of the CMA's budget until the CMA Board of Commissioner takes a particular decision related to their private interest, such as refraining from issuing an allegation of a suspected violation to a non-compliant firm.

Currently the CMA budget is supervised by the MOCI and the National Assembly, which review and approve the budget in accordance to Law No. 31 of 1978 regarding the organisation of public budgets under government supervision.<sup>364</sup> This proves that the CMA does not have independence in regulating financial services and stock markets. Scholars have highlighted the issue of attaching the CMA budget to the National Assembly as potentially leading to political influence on the CMA's decisions.<sup>365</sup>

Secondly, the Council of Ministers has influence over the CMA in relation to the allocation of financial resources.<sup>366</sup> The financial resources of the CMA consist of the following.<sup>367</sup>

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<sup>362</sup> Article 18 before the amendment No.75 of 2015

<sup>363</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68). 700.

<sup>364</sup> Ibid, 30

<sup>365</sup> Bader AlMullah, above, (n 62) 29. See also Adel AlManhea, above, (n 9) 25.

<sup>366</sup> Bader AlMullah, above (n 62) 29.

<sup>367</sup> Article 19 is amended pursuant to Law No. 22 of 2015 Amending Some Provisions of CML.

- 1) Fees and charges collected for the CMA by virtue of laws and regulations or organisational decisions issued by it.
- 2) All allocations to the CMA from the state's budget.
- 3) Revenues earned from the investment of the financial reserves of the CMA.
- 4) Fines imposed by the law by virtue of judicial rulings or decisions of the Disciplinary Board of the Authority.<sup>368</sup>
- 5) Funds from the settlement of criminal lawsuits filed regarding capital markets crimes.
- 6) Any other revenues stipulated by laws or bylaws.<sup>369</sup>

It seems that the CMA's budget is clearly attached to the state's budget. The current provisions in the CML regarding the CMA's financial resources make it impossible for it to operate without consent from the Council of Ministers.

Thirdly, in regard to the nature of CMA debt, all sums due from third parties to the CMA are considered public funds; they are treated as debts payable to the Public Treasury and shall be collected in accordance with the procedures of collecting outstanding debts for the Public Treasury.<sup>370</sup> The purpose of this provision is to ensure the efficient collection of the CMA's debts, but it also has the effect of ensuring that the CMA is financially connected to the Council of Ministers. To ensure the stability of the financial system, the CMA must have long-term financial reserves to cope with the systemic risk that exists in securities activities. The amount and means of creating such reserves shall be determined by a decision issued by the Council of Ministers, upon a proposal from the CMA Board. The CMA shall manage such reserves, and if these reserves reach the determined amount the surplus shall be transferred to the Public Treasury of the state. If at any time the reserves drop below the determined amount, the government shall supplement them and pay the amount that is lacking. The CMA shall also have predetermined operational capital of 40 million Kuwaiti dinars, from which the expenses of all CMA activities shall be paid. Expenses shall be paid and covered directly from the CMA's cash reserves, in accordance with CML and its Executive Bylaws. The CMA's capital may be increased through a decree.<sup>371</sup>

These provisions cause serious problems to the CMA in practice. The CMA Board's chair submits the annual budget and its appendices to the Board for approval. It is then sent to the

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<sup>368</sup> Executive Bylaws, Module two, Chapter Eight, Article 8.10.

<sup>369</sup> Ibid.

<sup>370</sup> CML, Article 20.

<sup>371</sup> Article 21 is amended pursuant to Law No. 75 of 2015 Amending Some Provisions of the CML.

Council of Ministers to be approved, and submitted to the legislative authority at least two months before the end of the financial year.<sup>372</sup> Hence the CMA cannot operate without the approval of the Council of Ministers; this may lead to delays in the budget process, because gaining the approval of the Council of Ministers has its own procedures and problems. It relies on the approval of the National Assembly, which may take quite a time. As the interviews confirmed (see below), a political bloc can influence MPs to withhold approval of the CMA's budget until they achieve their private goals. It is recommended that the CMA's budget should be separate and independent from the Council of Ministers. Since the CMA obtains income from the provision of fees and charges, as outlined above, this ought to be sufficient for the CMA to be able to cover all its financial needs without resorting to the Council of Ministers. The CMA can be self-funded by the industry through imposing fees and charges on all licensed firms and individuals. Currently, the CMA is not financially independent, thus it does not possess the capacity to act contrary to the Council of Ministers' desires. To bring the Kuwaiti regime into line with the IOSCO Principles, which state that the regulator should have adequate funding to exercise its powers and responsibilities, the current legal structure should be reformed. The CMA provisions are contrary to the IOSCO Principles because the CMA's budget is attached to and dependent upon the Council of Ministers' powers and budget. It is worth mentioning that the CMA does not regularly rely on the government for budgetary support, but the government may provide financial assistance to meet investment requirements. Accordingly, to improve the legal framework and enhance compliance with the IOSCO Principles, the CMA should be separately funded to safeguard its independent position.<sup>373</sup> In general, the CMA has enough resources to discharge its present duties.

The interviewees made contradictory statements about the attachment of the CMA's budget to the National Assembly, because their views rather depend on the position of the interviewee in the financial system.

One group sees the attachment of the CMA budget to the government and the National Assembly as having a huge impact on the independence of the CMA.

Participant No. 1 stated:

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<sup>372</sup> Executive Bylaws, Module two, Chapter Eight, Article 8.7.

<sup>373</sup> Marc Quintyn and Michael Taylor, *Should Financial Sector Regulators Be Independent?* (International Monetary Fund, 2004).



Previously the CMA's budget was regulated without obtaining the National Assembly's approval as a separate budget, to avoid any political influence. Political influences happened when MPs who have private interest decided not to sign or approve the budget until the CMA does whatever they asked them to do. This is why in the previous version of the law, we regulate the law to not obtain National Assembly approval. Currently, the National Assembly changed the law to ensure that the CMA budget gets their approval. The law should change to allow more independence of the CMA.

Participant No. 3 stated:

The 2015 amendments to the CML especially Article 19 was according to political pressure to serve private interests. The current article requires the CMA to get the National Assembly's approval, which is a window for political influence, this must be changed.

Participant No. 4 said:

The CMA's budget took huge debate in the 2015 amendments; I believe the CMA has to give some sacrifices to be under the National Assembly's approval in order to avoid political influence, to change Article 122 regarding manipulation. The CMA tried to use some balance between what they should give and take in terms of the amendments at that time.

Participant No. 6 stated:

The question should be 'does the National Assembly have has the capacity to review the CMA's budget and give their opinion in very complex matter' or it is just a way to influence the CMA's decision by delaying their budget approval?

In contrast, a second group sees the attachment of the CMA's budget as a normal procedure that does not affect the independence of the CMA.

Participant No. 2 said:

The CMA's budget is one of the critical issues: we tried to have an independent budget that does not need the National Assembly's approval, but this is an unusual situation and cannot continue. The CMA's budget must be attached to the government as part of the executive branch that is responsible to provide public services. The current situation provides the CMA with independence while considering the chairman of the CMA as the Minister of Finance in terms of reviewing and approving the CMA's budget. It means that the CMA can prepare and refer the CMA budget independently without any interfere from another government sector such as the Minister of Finance.

Participant No. 5 stated:

In terms of the CMA's budget, there is no problem with the approval of the National Assembly as any other public authorities need the National Assembly to approve; so far there is no issue from the National Assembly to reject the CMA's budget.

Clearly, it is difficult to admit that the 2015 amendments attaching the CMA's budget to National Assembly approval have had a negative impact on the independence of the CMA. However, the majority of the interviewees see this move as affecting their independence and giving political blocs more opportunity to influence CMA decisions. The literature review also confirmed that the independence of the financial regulator depends on budgetary resources as a core element in avoiding external influence on regulatory decisions.<sup>374</sup> Thus it is important to reform the current provision and not obligate the CMA to have National Assembly approval of its budget.

## **5. Regulator accountability**

A financial regulator should be independent in exercising its function, but at the same time accountable for the way it exercises its duties both politically and legally.<sup>375</sup> It is a balance between the two concepts of accountability and independence to obtain sufficient regulation of the financial sector. As required by a democratic oversight system, any public body should be accountable for its actions either to a minister or to parliament.<sup>376</sup> Thus the questions concern the nature of the public responsibilities of the financial regulator, and how the CMA is held to account in the Kuwaiti legal system.

In the UK approach the FCA has public responsibilities and liabilities which define the regulator's role in exercising its function and duties to achieve the regulatory objectives.<sup>377</sup> Its Code of Conduct sets out the framework for the FCA to exercise its duties.<sup>378</sup> It places

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<sup>374</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 500. Hussain Boaruki, 'Ten Important Points About the New Amendment of the Capital Markets Law' *AlQabas* (Kuwait, 23 April 2018) <<https://www.alanba.com.kw/ar/economy-news/553297/23-04-2015--هيئة-اسواق-المال>> accessed 24 January 2020

<sup>375</sup> Dalvinder Singh, 'Legal Accountability of Financial Regulators', in Dalvinder Singh, above (n 21) 183

<sup>376</sup> Dawn Oliver, 'Regulation, Democracy, and Democratic Oversight in the UK' in Dawn Oliver & Tony Prosser, 'The Regulatory State: Constitutional Implications' (Oxford University Press, 2010) 243

<sup>377</sup> Dalvinder Singh, 'Legal Accountability of Financial Regulators', in Dalvinder Singh, above, (n 21) 190

<sup>378</sup> The FCA, the Code of Conduct available at << <https://www.fca.org.uk/publication/corporate/code-of-conduct-for-non-executive-directors.pdf>>> accessed 18 March 2020.

responsibility for compliance with the Code of Conduct on the regulator and its staff.<sup>379</sup> The FCA also publishes its business plan and sector view on its website, outlining its objectives and priorities.<sup>380</sup> All of those practices are formal arrangement allowing people to pursue a claim of damages against the financial regulator for not meeting its obligations or breaching them. Individuals can ask the FCA for compensation for the failure of private firms or even the failure of the regulator to achieve its regulatory objectives (no such system exists in Kuwait, as discussed below).<sup>381</sup> The FCA procedures to allow people to pursue a claim of damages against the regulator is a tool that the industry uses to protect the markets and its interests. The Code of Conduct is the platform to hold a regulator to account. There is undoubtedly a significant relationship between legal development and the ability to call the regulator to account. It helps to ensure the effective accountability of the legal system.

On the other hand, the Code of Conduct also provides the FCA with immunity to protect it from abuse of power by third parties. It enables the regulator to exercise its duties with reasonable protection from any unnecessary lawsuit. In the view of HM Treasury:

Under the Financial Services Act 2012, the FCA cannot be sued for libel or damages unless it can be shown it has acted ‘in bad faith’ or unlawfully, according to the Treasury spokesman’s reading of the Human Rights Act 1998.<sup>382</sup>

In the Kuwaiti system the CMA has its Code of Conduct,<sup>383</sup> but it does not contain any legal mechanism to hold the regulator to account if it fails to achieve its objectives.<sup>384</sup> The only two mechanisms the Kuwaiti legal system recognises to call the CMA to account are either internally through the CMA Board of Commissioners<sup>385</sup> or externally through the Minister of

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<sup>379</sup> The FCA Code of Conduct available at <https://www.fca.org.uk/publication/corporate/fca-employee-handbook.pdf> accessed 18 March 2020.

<sup>380</sup> The FCA Business Plan 2018/2019 available at << <https://www.fca.org.uk/publication/business-plans/business-plan-2018-19.pdf>>> accessed 18 March 2020.

<sup>381</sup> Dalvinder Singh, ‘Legal Accountability of Financial Regulators’, in Dalvinder Singh, above, (n 21 **Error! Bookmark not defined.**) 188

<sup>382</sup> Damian Fantato. ‘HM Treasury: FCA immunity is sacrosanct’ (2014) available at <<https://www.ftadviser.com/2014/11/26/regulation/regulators/hm-treasury-fca-immunity-is-sacrosanct-waVENCgmEYNhbaIKv7a5N/article.html>> accessed 27 January 2020.

<sup>383</sup> Code of Conducts for Capital Markets Authority’s Commissioners, passed in the Board of Commissioners Meeting No. 23 of 2014, held on 5 November 2014, last amended on 10 August 2016 <<https://www.cma.gov.kw/documents/20622/385481/Charter+of+Code+of+Ethics+for+CMA+Commissioners+-+amended-10Aug2016.pdf/6d032fa6-bf9c-4859-9e84-a88d41dd39df>> accessed 18 March 2020.

<sup>384</sup> The CMA, The Code of Conduct available at <<https://www.cma.gov.kw/documents/20622/385481/Charter+of+Code+of+Ethics+for+CMA+Commissioners+-+amended-10Aug2016.pdf/6d032fa6-bf9c-4859-9e84-a88d41dd39df>> accessed 18 March 2020

<sup>385</sup> CML, Article 10.

Commerce and Industry, who is accountable to the National Assembly. The mechanisms<sup>386</sup> to call the commissioners to account internally are insufficient. There are vague provisions in CML Article 10 and the Code of Conduct regarding the vacating of a commissioner's seat in case of death, disability or resignation, or if the commissioner loses his/her capacity. A decree shall be issued to end a commissioner's tenure if a final judgment of bankruptcy is issued against him/her; if the commissioner is charged with a definitive crime related to breach of honour or trust or with a freedom-restricting penalty for a crime; if the commissioner does not attend three consecutive or six non-consecutive meetings without a good reason acceptable to the Board of Commissioners; if the commissioner violates the provisions of CML Articles 27 or 29 regarding business activities and confidentiality; or if the commissioner intentionally violates the Code of Conduct laid down by the Board of Commissioners during its inception to specify the conduct for commissioners.<sup>387</sup> It is notable that the purpose of these conditions is to protect the markets from unqualified commissioners. Their implementation should increase confidence and trust in the supervision procedures.

The key problem with these conditions is that in certain cases a commissioner will lose his/her capacity and seat on the Board of Commissioners without any provision for defence. It is of concern that an administrative decree can be issued by the CMA Board without any investigation to allow the commissioner to respond to the allegations. This procedure is contrary to IOSCO Principle 5, which seeks to ensure that proper processes of investigation are adopted to resolve any allegations of wrongdoing a commissioner may face. It is essential to protect a commissioner's right to defend himself/herself by using appropriate mechanisms. This argument leads to another important question: if a commissioner who lost his/her seat subsequently filed a case against the CMA and won, what would happen as a result of that decision? It seems there are two possible scenarios. In the first, the CMA would respect the judgment and reappoint the commissioner, but that raises further issues as to what would happen to the replacement commissioner who was appointed in the meantime to fill the vacancy. If the replacement remained, the Board of Commissioners would number six, not five, which seems to violate CML Article 6. If the CMA Board decided to release the new commissioner, that might lead to the filing of a case for compensation against the CMA. The second scenario is that the Board of Commissioners would refuse to recognise the decision and

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<sup>386</sup> CML, Article 10 and The CMA Code of Conducts.

<sup>387</sup> Article No. 10 is amended pursuant to Law No. 108 of 2014 Amending Some Provisions of the CML.

decline to reinstate the commissioner – a situation that would most likely result in the aggrieved commissioner filing a compensation case against the CMA. This would probably have a negative effect on the stability of the markets and the CMA’s effectiveness as a regulator. Thus it is vital that any commissioner faced with a complaint and possible removal has the right to defend himself/herself and present all the evidence by means of a thorough investigation, both to protect individual commissioners’ integrity and to protect the markets from rumours and unnecessary controversies.

There are unanswered questions as to how the Board of Commissioners will deal with the rules in the Code of Conduct which determine the moral expectations of commissioners. The Code of Conduct has a detailed list of rules by which the commissioners must abide. Pursuant to CML Article 10(e), an intentional violation of the code shall result in a decree being issued to end the commissioner’s membership, thereby leaving the seat vacant.<sup>388</sup> On the positive side, stringent enforcement of the code may mean that commissioners are prevented from taking inappropriate actions. However, there is also the potential that the commissioners will not be able to enjoy full freedom and independence without inappropriate – explicit or implicit – interference from the Executive Authority, which currently enjoys moral and familial dominance over the members of the board.<sup>389</sup> It is important to note that minutes of the meetings of the CMA Board of Commissioners are not published, which raises a concern about the transparency of the CMA. There is no specification or guidance about how the CMA Board will hold the regulator to account, and there is a debate about the enforceability of the Kuwaiti Code of Conduct. As the interviews reveal (see below), there is a lack of procedures to implement the Code of Conduct, and practice shows it is necessary to reform the code to include more clarification and proper mechanisms to hold a regulator to account. The current framework does not appear to guarantee independence and autonomy, and the spectre of executive interference remains a real threat.

Paradoxically, the Code of Conduct is criticised for not providing enough guarantees to protect the members of the Board of Commissioners. There is no protection against arbitrary procedures taken against members, but they are obliged to vote for resolutions with which they do not agree. The law states that a commissioner will lose his/her position and the post will

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<sup>388</sup> CML, Article 10(e).

<sup>389</sup> Nagham Al Dabbous, above (n 338) 117.

become vacant if, for example, the commissioner ‘intentionally violates the “Code of Conduct”’.<sup>390</sup> This clause raises many questions about accountability. Who will determine the procedures for deciding the outcome of this scenario? What are the procedures to call the commissioner to account? What are the guarantees afforded to a commissioner who has allegedly transgressed the Code of Conduct? Which authority has the right to issue a resolution removing the commissioner from his/her post on the CMA Board? The final clause of CML Article 10 specifies that the Board shall issue a resolution stating that the position of the commissioner is vacant, including the reason for the commissioner’s removal. Does the CMA Board have the power to do this, or would it be necessary to return to the Minister of Commerce and Industry, who supervises the Board? There is an administrative law, the rule of ‘equilibrium of competence and form’, which provides a legal tool to determine if the situation warrants a decree for issuing a resolution of appointment to a specific job or position. Does this decree make it possible for an employee to be removed from his/her position using this legal maxim? There is no clear provision within the law to determine how such a scenario would be resolved.<sup>391</sup> It is contended here that this lack of clarity as to how a commissioner might be removed for violating the Code of Conduct is further evidence of the need to reform the CML to ensure that it is aligned with best practices. In particular, it should be amended to ensure that the removal processes comply with IOSCO Principle 2, which states that the ‘The Regulator should be operationally independent and accountable in the exercise of its functions and powers.’ It is contended that as the law currently stands, and for the reasons outlined above, this principle has not yet been fully implemented within the Kuwaiti legal framework.

Another important element is that there is conflict of interest in applying the Code of Conduct because the same authority investigates a breach and issues the decision about the relevant commissioner. The commissioner might have influence over the other four commissioners of the CMA Board, with whom he/she works on day-to-day basis, thus it is necessary to ensure that any breach by a commissioner is investigated by a different authority. One interviewee highlights this issue, and suggests that the responsible authority to investigate a violation of the Code of Conduct must be a judicial committee consisting of judges and experts in the financial sector to ensure its fair and reasonable judgement (Participant No. 2, below).

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<sup>390</sup> CML, Article 10 (e).

<sup>391</sup> Ahmad Alenezi, “Fake Independence of Kuwait Stock Exchange Board of Commissioners”, 2012

The interviews clearly confirmed that the Code of Conducts is vague, and there is no actual accountability mechanism in the CMA framework.

Participant No. 1 said:

The only way to hold commissioners to account is through their Code of Conducts but there is no mechanism to implement this code and no investigation procedures for any kind of breach. The CMA Board must solve this issue internally. For example, the referral of the governor of the Central Bank of Kuwait to the prosecutor for insider dealing and the outcome of this investigation about his honesty did not lead to hold the commissioner to account. The CMA Board decided that there is no breach of the code based on the CMA Board decision.

Participant No. 2 stated:

The Code of Conducts is the only legal basis to hold a commissioner to account but there are no clear procedures on how the Board of the CMA holds the commissioners to account. It is extremely necessary to issue clear procedures to guide the CMA Board to hold a commissioner to account. It would be sufficient if the CMA law will allow the establishment of a judiciary committee to investigate a commissioner's violation. It would be a fair and unbiased committee because it consists of judges. The accountability of the CMA commissioners should not be in the government hands to ensure independence of the CMA, therefore having a committee that consists of judges is a good idea.

Participant No. 4 stated:

There is no accountability for the CMA Board, no one can judge them. The Code of Conducts is obviously ineffective. The only way to hold the commissioner for account is indirectly from the minister and is insufficient as well. In fact, there is no accountability mechanism in the Kuwait system to hold commissioners to account at all.

Participants Nos 3, 5, 6 and 7 did not answer this question for political and legal reasons.

From a risk-based approach perspective, the CMA should design its strategy to hold commissioners to account based on risk assessment. The responsibilities of the CMA commissioners must be clear to enable a commissioner to be held to account for a breach, so it is necessary to assess the effect of a commissioner's decision on achieving the regulatory goals. Based on that assessment, the CMA's responsibility is established and the Council of Ministers and the MOCI can call the CMA Board to account. This is how the risk-based approach works to protect the regulatory objectives. A perfect example of the lack of a clear accountability framework and mechanisms is the referral of the governor of the CBK to the prosecutor for

insider trading in stock markets. The prosecutor's investigation found that the CBK governor was innocent and no insider trading had been committed. This event did not lead to the CMA Board of Commissioners being held to account due the lack of accountability mechanisms in the Kuwait legal system. If the risk-based approach is applied, the responsibilities of the CMA Board of Commissioners will be determined based on the effect of the referral and its risk of damaging the achievement of the regulatory goals. The application of the risk-based approach can ensure that the commissioners are held accountable for their actions. The referral of the governor of the CBK to the prosecutor is discussed further in the following sections.

The next sections explain how regulatory accountability works in Kuwait. In simple terms, to whom should one report if one wishes to call the CMA to account? The first authority is the MOCI. Transparency has also been increased by requiring the CMA to submit annual reports on its work to the competent minister.<sup>392</sup>

### 5.1 Ministry of Commerce and Industry

A complex and specialised activity like the organisation of financial market supervision calls for several accountability mechanisms. There are different categories of accountability arrangements, and an effective set of mechanisms should contain a balanced mix of *ex ante* and *ex post* accountability.<sup>393</sup> *Ex post* accountability refers to reporting after actions have been taken, for example in annual reports. This is an important factor in ensuring transparency in the financial markets, and also a supervisory tool to enable the Council of Ministers and the MOCI to oversee the CMA's role.

Transparency is one of the main objectives that the Council of Ministers and the CMA are trying to achieve. In pursuit of this, within 120 days after the end of every financial year, the CMA must present to the MOCI an annual report on its activities, work and achievements in the growth and development of the markets during the completed year, including the CMA's financial accounts and the auditor's report.<sup>394</sup> The annual report is then submitted to the Council of Ministers.<sup>395</sup> Thus the Council of Ministers has oversight of the CMA's operations, but the question is, does the Minister of Commerce and Industry or the Council of Ministers have the

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<sup>392</sup> Asim Jusic and Farah Yassen, above (n 30) 55.

<sup>393</sup> Eva Hüpkes, Marc Quintyn and Michael Taylor, above, (n 16) 6.

<sup>394</sup> CML, Article 25

<sup>395</sup> Article 25 is amended pursuant to Law No. 75 of 2015 Amending Some Provisions of CML.



power to investigate or examine the CMA's policies? The CML provides overlapping provisions which render it difficult to define the responsibilities of the CMA Board of Commissioners. From a risk-based approach perspective, if the CMA has not achieved its regulatory objectives, the stability of the economy can potentially be affected. For example, if the CMA did not achieve its fifth objective as stated in the CML, which is to prevent insider trading, this risk will affect the whole economy and destroy investor trust in the market. In this sense the minister and the Council of Ministers should act based on the impact of the CMA's decision on achieving the regulatory objectives to protect the economy.

The Council of Ministers has means by which to influence the CMA because it is associated with the Minister of Commerce and Industry – who is a member of the Council of Ministers.<sup>396</sup> The Prime Minister is the chair of the Council of Ministers. The main ministers related to the CMA are those of Commerce and Industry and Finance. The CMA may also be affected by political influence through the process of parliamentary oversight regarding the Minister of Commerce and Industry. Furthermore, according to Article 99 of the Kuwait Constitution, the Kuwait National Assembly practises parliamentary oversight through *ex post* soft mechanisms such as parliamentary questions and committees, and the hard mechanism of parliamentary investigation that can result in a finding of individual ministerial responsibility.<sup>397</sup> As explained previously, the CMA objectives and annual review are descriptive and do not give any practical indications of the achievement of the objectives. There is no real method to call the CMA to account by either the MOCI or the Council of Ministers.

In the UK the Treasury retains overall responsibility for the activities of the FCA and the financial markets. The FCA's relationship with the Treasury is outlined in an MoU.<sup>398</sup> The Treasury has a number of controls over the FCA: the FCA submits its annual report to the Treasury for examination, and it is then the responsibility of the Treasury to submit that report to parliament.<sup>399</sup> The reporting procedures in both the UK and Kuwait follow a similar process, but the main difference is the ability to call the regulator to account. In UK there are clear tools and mechanisms to enforce effective accountability, while in Kuwait it seems there is no legal

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<sup>396</sup> The Council of Ministers is part of the executive branch of government. Pursuant to Article 52 of the Kuwait Constitution, the Executive consists of the Amir, the Cabinet and the Ministers.

<sup>397</sup> Kuwait Constitution, Articles 99-101. See Asim Jusic and Farah Yassen, above (n 30) 50.

<sup>398</sup> Bank of England (1997/98) Memorandum of Understanding between HM Treasury, The Bank of England and the FSA (MoU), Banking Act Report, 37–39.

<sup>399</sup> Dalvinder Singh, above (n 21) **Error! Bookmark not defined.** 16.

framework to determine the commissioners' responsibility and a lack of mechanisms to call the commissioners to account. Apart from the MOCI and the Council of Ministers, the CMA is indirectly accountable to the National Assembly through the Minister of Commerce and Industry,<sup>400</sup> as discussed above.

## 5.2 National Assembly

As mentioned, the CMA reports to the MOCI, which is in turn accountable to the National Assembly. The issue here is the effectiveness of this mechanism to hold the CMA commissioners to account, and how it works in practice. The National Assembly is Kuwait's legislature. It is responsible for issuing laws and supervising the Council of Ministers. In its supervisory role over the Council of Ministers, the National Assembly has the power to remove government ministers from their positions. Under the Kuwaiti model of constrained parliamentarianism, the CMA is a government-led administrative regulator with limited accountability.<sup>401</sup> The National Assembly does not have a direct relationship with the CMA, but there is indirect accountability through the relevant minister and the Council of Ministers. There is a need to reconsider the role of the National Assembly regarding supervision of the CMA.<sup>402</sup> One scholar suggested that to increase the independence of the CMA and minimise the Council of Ministers' influence, the CMA should be directly responsible to the National Assembly.<sup>403</sup> In fact, this suggestion does not increase the independence of the CMA, and it is inadvisable to attach supervision of the CMA directly to the National Assembly for many reasons. First, the National Assembly does not have the capacity to review the CMA's work because it deals with specific matters related to the financial sector that need expert knowledge to evaluate. Secondly, such a situation does not apply the constitutional principle of 'separation of powers', because the CMA is part of the government as an executive branch to provide public service. The government is responsible for providing public services while the National Assembly is responsible for supervising government to ensure the best services are provided

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<sup>400</sup> Asim Jusic and Farah Yassen, above (n 30) 65.

<sup>401</sup> Yousry Al-Assar, 'The legal system of the Capital Markets Authority and its effectiveness in achieving its objectives: case studies of Egypt, France and Kuwait' (2016) 4 (15) *Kuwait International Law School Journal* 33. See also Asim Jusic and Farah Yassen, above, (n 30) 37.

<sup>402</sup> Asim Jusic and Farah Yassen, above (n 30) 60.

<sup>403</sup> Nagham Al Dabbous, above (n 338) 190.

to citizen and to issue laws to serve the public interest.<sup>404</sup> The interviewees also felt that the National Assembly cannot be the entity responsible for supervising the CMA.

Participant No. 1 said:

Kuwait's system does not allow the CMA to be attached to the National Assembly as direct supervision because the government must manage public services and achieve public interest. On the other hand, the National Assembly role is to issue and supervise the government. The government/executive is more capable of administrative roles in the country than the National Assembly.

Participant No. 2 stated:

From my experience, I can say the National Assembly is unable to have direct supervision over the CMA due to lack of expertise in MPs.

Participant No. 3 said:

I don't see any public service authority that can be attached to direct supervision of the National Assembly due to the separation of power principle.

Participant No. 4 stated:

We don't want to put the CMA in a worse position by allowing direct political influence on the CMA's decisions.

Participant No. 5 stated:

The solution cannot be the attachment of the CMA to the National Assembly. It will make the situation worse by allowing political influence.

Participant No. 6 said:

It could be an open gate for another issue who will hold the National Assembly to account if they did not supervise the CMA correctly.

Participant No. 7 said:

The separation of power principle does not allow this kind of supervision; the CMA must be a part of government to provide public services.

The clearest example of the lack of CMA accountability was when the CMA Board referred the governor of the CBK to the Capital Market Prosecutor on a charge of insider trading.<sup>405</sup>

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<sup>404</sup> Article 50 of Kuwait Constitutional Law

<sup>405</sup> 'The CMA referred the Governor of the CBK to Prosecutor' (5 February 2015) Al-Jarida Newspaper available at << <https://www.aljarida.com/articles/1462412784275351800/>>> accessed 18 March 2020.

After investigation, the prosecutor dismissed the case due to lack of evidence and no crime was committed. The impact of this referral of the CBK governor had a huge effect on Kuwait's economy, and damaged trust and confidence in the stock markets – insider trading is a serious allegation, especially for an official like the governor of the CBK. When the CMA was unable to proceed with its charge, which body should be held responsible for the detrimental effect? The only way to hold the CMA's Board of Commissioners to account is through the Code of Conduct, which states clearly that if a commissioner intentionally violates the Code of Conduct, his/her seat will be vacated by decree of the CMA Board. The referral of the CBK governor violates the Code of Conduct because it affects the regulatory objective of protecting the markets. CML Article 10 clearly states that the commissioners should be held responsible if they take a decision that affects the Kuwait economy badly, and the referral of the governor of the CBK damaged investor trust in Kuwait's economy, therefore the CMA Board of Commissioners shall hold to account. Accordingly, one MP questioned the Minister of Commerce and Industry about the responsibility of the CMA Board of Commissioners regarding the unjustifiable referral and its detrimental effects.<sup>406</sup> The minister responded briefly to the MP without any explanation of the underlying policy. Furthermore, the Protection of Public Funds Committee at the National Assembly issued a report recommending that four of the Board of Commissioners' seats must be vacated due to violations of the Code of Conduct,<sup>407</sup> but there is no rule to oblige the Minister of Commerce and Industry to follow the guidance of the committee. It appears that the command-and-control system is working in this situation: there seems to be a separation of power and parliament can call the minister to account, but in practice it is the classical theme of command and control.

This analysis proves that there is no effective accountability relationship between the CMA and the National Assembly, which leads us to the core principle of the command-and-control system: the government has absolute powers. For that reason, some scholars have categorised the CMA as a 'government-led' administrative regulator.<sup>408</sup> Although the minister has only

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<sup>406</sup> Omar AlTabtabea asking AlRoudhan About Capital Markets Authority decision to refer the governor of the Central of Kuwait to Prosecutor' *Alwasat newspaper*, Kuwait, 19 March 2017) <[www.alwasat.com.kw/ArticleDetail.aspx?id=30090](http://www.alwasat.com.kw/ArticleDetail.aspx?id=30090)> accessed 18 March 2020

<sup>407</sup> The report stated that there was clear intention by four of the CMA's Board to refer the Governor of the CBK to the Capital Market prosecutor with the existence of internal legal opinion from legal department confirming that there is no violation of the insider trading provision by the governor. available at <<https://alqabas.com/467910/>> accessed on 27 January 2020.

<sup>408</sup> Asim Jusic and Farah Yassen, Above, (n 30) 66.

limited supervisory power and lacks full control over CMA policy,<sup>409</sup> responsibility will nonetheless rest on his shoulders. The lack of clarity regarding ministerial responsibility makes it hard to distinguish the responsibility for each body or decision.

The current institutional position of the CMA shows that there is no reliable model for making it accountable for its policy because either the National Assembly or the concerned minister can call the CMA to account. This can be defined as constrained parliamentarianism,<sup>410</sup> which is a system that attempts to temper the power of the government by granting independence to a variety of balancing institutions, such as the capital markets regulator. The CMA's position of limited accountability has no clear place in an oversight system based on separation of powers. The parliamentary tools and oversight mechanisms can have an impact by decreasing the independence of the CMA and the quality of regulation without increasing its accountability.<sup>411</sup> Furthermore, the constitutional principle of checks and balances must be applicable in all events, because each branch of government has its own distinct obligations and responsibilities to fulfil. The independence of the CMA must not conflict with constitutional principles between the three branches legislative, executive and judicial. Clearly, the effectiveness of regulation depends on the ability of the regulator to carry out its role, thus it is necessary to adopt a new law to clarify the supervisory responsibility. One suggestion is to assign direct 'joint and several' *ex post* responsibility to the chair of the CMA Board of Commissioners and the responsible minister before the National Assembly.<sup>412</sup> Although this suggestion has some merit, it is inadvisable to have joint and several *ex post* responsibility because it will lead to more political influence and thus make the situation even worse. A risk-based approach offers an alternative mechanism to ensure that the CMA exercises its functions and is accountable for its actions. The risk-based framework defines the regulator's choices of what types of failures are linked to its priorities<sup>413</sup> and determines what the CMA should be accountable for. The adoption of a risk-based approach involves both managerial and political accountability;<sup>414</sup> it involves developing decision-marking procedures to prioritise regulatory

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<sup>409</sup> Ibid.

<sup>410</sup> Ibid. 36.

<sup>411</sup> Ibid. 70.

<sup>412</sup> Ibid. 35.

<sup>413</sup> Ibid. 20.

<sup>414</sup> Julia Black, above, (n 99) 2.

<sup>414</sup> Julia Black, 'Tensions in the Regulatory State', (Public Law, 2007) 7.

activities, and deploying resources.<sup>415</sup> It is a matter of choices, where the regulator identifies the risks and deploys its resources accordingly. There is space for judgement to decide which risk is the most significant for the regulator's objectives and to act to mitigate this risk.<sup>416</sup> So the regulator's choices determine its responsibility. Furthermore, to have effective accountability procedures the establishment of an independent committee is suggested to investigate any violation or breach of the Code of Conduct by the CMA's Board of Commissioners. The committee must consist of judges appointed by the judiciary branch to guarantee there is no conflict of interest in the appointment process.

## **6. Conclusion**

This chapter shows how the promulgation of the CML, Law No. 7 of 2010, has improved the regulation of Kuwaiti financial services and stock markets. The law states the CMA's objectives, complying with international standards to set clear objectives. It also fulfils the need to set objectives within a risk-based approach, to enable the regulator to establish its priorities based on risk. However, there is no appropriate mechanism to achieve the objectives. The rules are descriptive, and further guidance and adoptive policy are required to implement them.

The chapter analyses the Kuwait legal structure in terms of the CMA's independence and accountability. It reveals that while some progress has been made in the recent past with regard to the regulatory and institutional aspects of supervision of securities markets, the underlying legal framework remains inadequate and needs improvement. The independence of the CMA cannot be achieved without the tools and powers to appoint the CMA Board of Commissioners independent of government and political influence. The MOCI's power over the CMA allows great influence by the government and political parties in the process of appointing the commissioners. The procedures must be changed to involve private sector actors in the appointment process. Commissioners' remuneration is another indication of a lack of CMA independence: the Council of Ministers determines the commissioners' salaries, which has an enormous effect on the independence of the CMA. Finally, the attachment of the CMA budget to the government budget and its financial support to the CMA show that the CMA does not have appropriate independence. There must be reform to adopt more appropriate mechanisms to give the CMA enough independence to supervise and enforce the law in the financial sector.

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<sup>415</sup> Julia Black, above, (n 99) 3.

<sup>416</sup> *ibid.* 13.

The CMA does not have effective accountability tools and powers to hold a commissioner to account for a breach. The analysis shows the lack of accountability mechanisms in practice. The Code of Conduct does not contain procedures and rules to hold commissioners to account for their decisions and activities. There is no published policy to set the framework for the CMA Board of Commissioners' responsibilities. A suggestion is to use a risk-based approach to set CMA responsibilities and liabilities in working to achieve its objectives. This approach can be used as a methodology to determine the CMA's responsibilities based on risk. The accountability mechanism will be clear and sound, which will eventually improve the CMA's abilities to protect the markets.

## Chapter 5: Enforcement in Financial Regulation <sup>417</sup>

### 1. Introduction

The robust enforcement of securities laws is fundamental to help enhance investor confidence and maintain fair and efficient markets.<sup>418</sup> The enforcement regime has two arms to enforce financial regulation, namely the regulator and the courts.<sup>419</sup> This research focuses only on the regulator.

The term ‘enforcement’ should be interpreted broadly enough to encompass ‘powers of inspection, investigation and surveillance such that the regulator should be expected to have the ability, the means, and a variety of measures to detect, deter, enforce, sanction, redress and correct violations of securities laws’.<sup>420</sup> There are obvious benefits to having adequate enforcement tools: a financial regulator that is properly equipped will help to impede operations of risky practice and products.<sup>421</sup> One way of looking at it is to view the supervision rules as the eyes with which the financial regulator observes the market and the enforcement tools as the hands of the regulator to ensure compliance with the rules. It must be noted that both supervision and enforcement must work in the same manner to protect financial stability: light supervision with strong enforcement cannot protect the markets. Both must work in tandem to achieve the law’s objectives.<sup>422</sup> This means that the financial regulator has the tools to gather information and the power to ensure that rules and regulations are followed, and in case of any breach of these rules the regulator has the ability to punish and deter the violator. It is necessary to have high-quality regulation with strong enforcement.<sup>423</sup> Enforcement is key to the

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<sup>417</sup> An early version of this chapter was published in the Kuwait International Law School Journal in October 2018, special edition No. 3.- Part 2. Available at <<https://journal.kilaw.edu.kw/wp-content/uploads/2018/12/101-144Lulwa-M.-Al-Ben-Ali.pdf>>> accessed 18 March 2020.

<sup>418</sup> IOSCO, ‘Methodology For Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation’ (May 2017) 63. <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>>> accessed 27 January 2020.

<sup>419</sup> Ibid. See also Florencio Lopez-de-Silanes, ‘A Survey of Securities Laws and Enforcement,’ (Policy Research Working Paper 3405, World Bank, September 2004) 4.

<sup>420</sup> IOSCO, ‘Methodology For Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation’ (May 2017) 63. <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>>> accessed 27 January 2020.

<sup>421</sup> Bashar Alghanim, ‘The Implications of Financial Regulation for Kuwait’s Financial Sector’, (8<sup>th</sup> Annual Conference of the EuriMed Academy of Business, Italy, 2011) 137, 140 <<http://emrbi.org/wp-content/uploads/2015/11/euromed2015-book-of-proceedings-2015-11-02.pdf>> accessed 27 January 2020.

<sup>422</sup> Robert Baldwin and Julia Black ‘Really Responsive Regulation’ above (n 226) 60-62.

<sup>423</sup> Luca Enriques and Sergio Gilotta, *Disclosure and Financial Market Regulation* in Niamh Moloney, Eilis Ferran, Jennifer Payne, *The Oxford Handbook of Financial Regulation* (Oxford University Press 2015) 527.



credibility of regulators and fosters the achievement of all the objectives of securities regulation: investor protection, fair markets and financial stability.<sup>424</sup>

The implementation of effective enforcement programmes has been very challenging for all regulators since the financial crisis in 2008. The crisis exposed the failure of financial regulators.<sup>425</sup> One of the reasons for that failure was that enforcement tools were not effective enough to control excessive risk, nor did they have the capacity to protect the markets.<sup>426</sup> It has been noted that one weakness of the FSA was that it rarely fined or banned senior executives prior the 2008 financial crisis.<sup>427</sup> Regulatory enforcement in Kuwait suffers from various weaknesses, among which is poor-quality action.<sup>428</sup> Lax enforcement decisions against false, incorrect or delayed disclosure by listed companies in stock markets will eventually lead to insider trading. Thus it is important to give financial regulators sufficient enforcement tools to punish non-compliant listed companies which do not disclose material information correctly in order to prevent insider trading in stock markets. It is no exaggeration to conclude that effective regulation needs strong enforcement.

There are different strategies and approaches to enforcing the law in the financial sector.<sup>429</sup> The regulator uses its inspection and investigative powers to ensure compliance with regulations related to securities activities, and more specifically to prevent the use of insider information. Consequently, the regulator carries out inspections and investigations and takes enforcement

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<sup>424</sup> Ana Carjaval and Jennifer Elliott, 'The Challenge of Enforcement in Securities Markets: Mission Impossible?' (August 2009) IMF Working Paper WP/09/168, 4 <<<https://www.imf.org/external/pubs/ft/wp/2009/wp09168.pdf>>> accessed 27 January 2020.

<sup>425</sup> Julia Black, 'The Regulatory Styles and Supervisory Strategies' above (n80) 223.

<sup>426</sup> Gerard Caprio, 'Financial regulation after the crisis: how did we get here, and how do we get out?' (2013) 16 <<http://www.lse.ac.uk/fmg/workingPapers/specialPapers/PDF/sp226.pdf>> accessed 27 January 2020. See also Niamh Moloney, Eilis Ferran, Jennifer Payne, *The Oxford Handbook of Financial Regulation* (Oxford University Press 2015) 281, see Michael Ioannides 'Europe's new transformations: how the EU economic constitution changed during the Eurozone crisis' (2016) 53(5) C.M.L. Rev. 1237, 1282, re European banking regulation and stability.

<sup>427</sup> Alison Lui, 'Protecting whistle-blowers in the UK financial industry' (2014) 11 International Journal of Disclosure and Governance 195, 202.

<sup>428</sup> Mohammad E Al-Wasmi, 'Corporate Governance Practice in the GCC: Kuwait as a Case Study' (PhD thesis, Brunel University 2011). 45, 233.

<sup>429</sup> Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate* (Oxford University Press, USA 1992) 20-25, see also OECD Regulatory Enforcement and Inspections, OECD Best Practice Principles for Regulatory Policy, (OECD, 2014) available <<http://dx.doi.org/10.1787/9789264208117-en>> accessed 27 January 2020. See Niamh Moloney, Eilis Ferran, Jennifer Payne, *The Oxford Handbook of Financial Regulation* (Oxford University Press 2015)

action against non-compliant firms by using a disciplinary/civil regime, or a criminal regime by referring the matter to the prosecutor.

This chapter examines the power of the CMA under CML regulations to detect and punish non-compliant firms. It begins with the power of investigation, including gathering data by either requesting information or on-site visits. One of the tools for gathering information is the whistleblowing regime, discussed in Chapter 8. This chapter assesses the CMA's administrative enforcement power and identifies best practices to detect and punish the non-compliant.

## 2. Enforcement policy

There are two main enforcement approaches: compliance and deterrence.<sup>430</sup> Both approaches require specific tools and procedures for effective enforcement. There has been much dispute between proponents of these two approaches.<sup>431</sup> The advocates of deterrence argue that the compliance of firms cannot be achieved without strong sanctions, while those favouring compliance argue that persuasion and cooperation are the best way to ensure compliance.<sup>432</sup> The deterrence approach alone cannot be effective to ensure compliance; for example, in a deterrence-oriented strategy a firm may choose the lowest-cost option and hence evade rather than comply with the law because the cost of deterrence (often a financial penalty) is less than the expected cost of compliance.<sup>433</sup> On the other hand, supporters of compliance identify several reasons why this approach is superior to deterrence. First, monitoring costs are high and it is difficult to detect non-compliant firms.<sup>434</sup> Secondly, when violations are detected there should be sufficient evidence to convict the firm; as experience has shown, this is difficult to obtain. Finally, court and prosecution costs are high, and sanctions tend to be low compared with the high costs of compliance. Thus a combination of both approaches will probably be the most effective method of enforcement,<sup>435</sup> and developed countries tend to adopt such a

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<sup>430</sup> Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate* above (n 429) 20-25, see also Julia Black, *Rules and Regulators*, (Oxford University Press 1997) 41. See also John T Scholz, 'Voluntary Compliance and Regulatory Enforcement' (1984) 6 *Law & Policy* 385, .385-386.

<sup>431</sup> Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate* above (n 429) 5-6, 20-21.

<sup>432</sup> *ibid.* 20-25. Julia Black and Robert Baldwin, above (n 226) 59- 62.

<sup>433</sup> John Scholz, 'Voluntary Compliance and Regulatory Enforcement' above, (n 430) 389.

<sup>434</sup> John T Scholz, 'Voluntary Compliance and Regulatory Enforcement' above, (n 430) 392. See also Dalvinder Singh, above, (n 21) 115.

<sup>435</sup> Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate* above (n 429) 24, see also Dalvinder Singh, above (n 21) 114. See OECD *Regulatory*

combination in their enforcement policy.<sup>436</sup> A responsive regulatory theory employs a balance between compliance and deterrence approaches.<sup>437</sup>

In 1992 Ayres and Braithwaite published *Responsive Regulation*, an important book outlining how a regulatory approach can promote compliance.<sup>438</sup> It presents a model which persuades and encourages firms to comply with the law and uses escalation to punish violators. As the authors<sup>439</sup> explain:

The idea of when to punish and when to persuade? To reject punitive regulation is naïve, to be totally committed to it is to lead a charge of the Light Brigade.

The idea of this theory is a balance between deterrence and compliance where each firm complies with the law, but if a firm defects from cooperation the regulator uses deterrence and enforces fines and penalties. The deterrence and compliance models rely on a tit-for-tat approach. Once firms agree to cooperate, the supervisory regulator does the same; and the regulator's response depends on how the firms act.

It is worth mentioning that Ayres and Braithwaite developed two enforcement pyramids: one to be applied by governments to entire industries, and one for regulators to apply to individual regulatees. These pyramids help to improve the strategy to enforce the law. The contribution of this theory is in recognising the different reasons or motivations for firms or individuals to comply with the law, which Ayres and Braithwaite call 'multiple selves'. There are plural motivations for compliance and non-compliance that firms and individuals consider when applying the law.<sup>440</sup> Each of these motivations interacts with the different approaches. This theory works on an 'organisational hierarchy', with more cooperative strategies at the base of the pyramid and more punitive approaches gradually being used only when cooperative strategies fail.<sup>441</sup> The regulator presumes that firms and individuals are being cooperative, but if something comes up showing that the regulatees are not cooperative, the regulator uses its

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*Enforcement and Inspections*, OECD Best Practice Principles for Regulatory Policy, (OECD 2014) available <<http://dx.doi.org/10.1787/9789264208117-en>> accessed 27 January 2020. 34.

<sup>436</sup> OECD, *Regulatory Enforcement and Inspections*, OECD Best Practice Principles for Regulatory Policy, (OECD 2014) available <<http://dx.doi.org/10.1787/9789264208117-en>> accessed 27 January 2020.

<sup>437</sup> Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate* above (n 429) 24.

<sup>438</sup> *ibid.* 35.

<sup>439</sup> *ibid.* 21, 35.

<sup>440</sup> *ibid.* 31.

<sup>441</sup> *ibid.* 34-35, 52.

tools and power to deter non-compliance. If the firms and individuals return to compliance, their change of attitude should be rewarded with less harsh enforcement. In other words, the regulator should forgive non-compliant regulatees if they are willing to cooperate again.

The regulatory approach begins at the bottom of the pyramid and escalates in response to compliance failures<sup>442</sup> (see Figure 1). The regulator should explore a range of approaches to encourage compliance, but should also be prepared to escalate a sanction when a firm fails to comply. Escalation occurs when dialogue fails, and de-escalation rewards a positive response. For example, if regulatees behave well and comply with the law as the regulator desires then there will be a de-escalation of regulatory activity down the pyramid. This is a tit-for-tat approach, as explained above. It provides fairness and improves the outcome. Regulatees are encouraged to comply with the law again, and gain benefits from their compliance. Scholars have explored the motives for compliance: some cite self-interest as the reason for obeying the law,<sup>443</sup> while others rely on normative and social reasons.<sup>444</sup> Some scholars have created new ideas for responsive regulation, for example ‘flexible enforcement’.<sup>445</sup> All these improvements can lead to better understanding of best practice in regulating the financial markets.



<sup>442</sup> *ibid.* 35. See also Julia Black and Robert Baldwin, 'Really Responsive Risk-Based Regulation' above (n 226) 5-9.

<sup>443</sup> John T Scholz, 'Voluntary Compliance and Regulatory Enforcement', above, (n 430) 388, See Neal Shover and Andy Hochstetler, *Choosing White-Collar Crime* (Cambridge University Press 2006) 56, 72. Tom Tyler, *Why People Obey the Law* (Princeton University Press 2006) 3-5

<sup>444</sup> Tom Tyler, *Why People Obey the Law* (Princeton University Press 2006) 3-5 John T Scholz, 'Voluntary Compliance and Regulatory Enforcement', above, (n 430) 388

<sup>445</sup> John Scholaz 'Cooperative Regulatory Enforcement and the Politics of Administrative Effectiveness' (1991) vol.85 *American Political Science Review*, 115, 118, See also Kagan 1994, p.387, John T Scholz, 'Voluntary Compliance and Regulatory Enforcement', above, (n 430) 391

Figure 1: The original enforcement pyramid as presented in Ayres and Braithwaite (1992)

However, scholars critique the responsive regulation approach in the context of developed economies. Black explains the limitations involved in rule-making decisions.<sup>446</sup> The main criticisms can be divided into three groups: the policy or conceptual, the practical and the principled.<sup>447</sup> Responsive regulation is not suitable for all cases. For instance, some risks cannot be covered by this approach. Furthermore, the expectation of responsive regulation that there is an ongoing relationship and dialogue between regulator and regulatees is not always applicable in practice. For example, in complex regimes with multiple regulators it is impossible to have ongoing dialogues and communication with all the regulatees. Finally, the regulators are not able to move up and down the pyramid easily.<sup>448</sup> It requires equal measures of violations and imposed sanctions followed by the appropriate regulatory activity to escalate or de-escalate the pyramid. It is important to highlight that this approach has not been examined in financial fields, and the enforcement pyramid is a two-key player with a rationale that dialogue and persuasion will be more fruitful than reaching the pyramid top.<sup>449</sup>

The important question for this research is whether the compliance approach will help to prevent insider trading in stock markets. The truth is that the persuasion method fails to prevent insider trading because insiders care more about gaining easy and illicit profit rather than compliance with rules.<sup>450</sup> The insiders are, in most cases, senior managers in companies who are motivated by profits and personal interest. They will not be stopped by persuasion methods or tools unless the cost of punishment exceeds the expected gain.<sup>451</sup> It is all about calculation of the profits and losses for insiders rather than the moral motivation to comply with the law. In fact, combining the two approaches to deter insider trading in stock markets is essential to create an effective enforcement strategy to prevent listed companies from concealing material information.<sup>452</sup> A strong disclosure regime is the first step to prevent the use of inside

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<sup>446</sup> Julia Black, *Rules and Regulators*, above (n 430) 6.

<sup>447</sup> Robert Baldwin and Julia Black, 'Really Responsive Regulation' above (n 226) 62.

<sup>448</sup> *ibid.* 63.

<sup>449</sup> *ibid.* 64.

<sup>450</sup> Richard Posner, 'An Economic Theory of the Criminal Law' (1985) 85 *Columbia Law Review*, 1193.

<sup>451</sup> Gary Becker, 'Crime and Punishment: An Economic Approach' (1968) 76 *Journal of Political Economy* 1, 9, 13.

<sup>452</sup> OECD, *Regulatory Enforcement and Inspections*, OECD Best Practice Principles for Regulatory Policy, (OECD 2014) available. <<http://dx.doi.org/10.1787/9789264208117-en>> accessed 27 January 2020

Ian Ayres and John Braithwaite, *Responsive regulation: Transcending the deregulation debate*, above (n 435) 35

information in stock markets, thus it is necessary to give the CMA sufficient tools and powers to ensure accurate disclosure and deter non-compliant companies.

The CMA used to rely only on a deterrence approach to enforce the law, but recently it has changed its policy.<sup>453</sup> In 2019 for the first time the CMA issued internal inspection guidance announcing its strategy to adopt compliance and risk-based approaches.<sup>454</sup> The CMA uses a combination of compliance and deterrence approaches to investigate firms. This combination of approaches improves the CMA's ability to use its resources to focus on the firms presenting the highest risk to its regulatory objectives.<sup>455</sup> This is similar to the FCA approach,<sup>456</sup> and prioritises limited resources in the areas that pose the greatest threat to the statutory objectives. Risk-based regulation provides a strategy for regulators to categorise regulated firms by risk-based assessment. The risk assessment scores and ranks each risk that entities face while carrying out their financial activities. After the risks are identified, each entity is ranked, and regulatory agencies deal with the entities based on this assessment. Risk-based regulation helps regulators to prioritise their efforts, but offers less assistance in identifying the kind of intervention needed to secure compliance.<sup>457</sup> The risk-based approach moves away from post-event rule-based regulation that focuses on non-compliance to create a flexible and targeted strategy focusing on risk and proactively supervising and enforcing financial regulation.<sup>458</sup> It helps to reveal non-compliant firms which do not disclose material information in stock markets. Gordon Brown described his vision of the implementation of a risk-based investigation and enforcement regime: 'No inspection, no form filling, no information required without justification, not just a light touch but a limited touch...'<sup>459</sup> It is a policy where the regulator can target its resources to the most needy areas.<sup>460</sup>

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<sup>453</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>454</sup> *ibid.* 11.

<sup>455</sup> *ibid.*

<sup>456</sup> The FCA Enforcement Guide (1/4/2014) s.2.3, see also The Financial Conduct Authority, 'How the FCA will investigate and report on regulatory failure' available at <<<https://www.fca.org.uk/publication/corporate/how-fca-will-investigate-and-report-regulatory-failure.pdf>>> accessed 28 January 2020.

<sup>457</sup> Julia Black and Robert Baldwin, 'Really Responsive Regulation' above (n 226) 66.

<sup>458</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) 5 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 28 January 2020.

<sup>459</sup> Gordon Brown Speech to CBI, Full text of Gordon Brown's speech to the annual conference of the Confederation of British Industry in London, *Financial Times* (November 28 2005) available <<<https://www.ft.com/content/9073a120-600d-11da-a3a6-0000779e2340>>> accessed 28 January 2020.

<sup>460</sup> Julia Black, 'The Development of Risk Based Regulation in Financial Services: Canada, the UK and Australia', above, (n 167)

In Kuwait, prior to the production of the CMA's internal inspection guidance there were no requirements in terms of scope of investigations.<sup>461</sup> Investigative action will generally be taken in all cases that come to the CMA's attention involving a breach of the CML. It undertaken administrative investigations of violations covered by the CML and its Executive Bylaws. The CMA had not published its guidance, which meant there was no public policy on conducting an investigation. The lack of clarity affected the application of a compliance approach, because it is based on persuasion and dialogue with the regulated entities.

After the issue of its internal inspection guidance in June 2019, the CMA adopted a compliance and risk-based approach.<sup>462</sup> The on-site inspection department uses risk assessments to create listed companies' profiles. Based on those profiles and the risk scores, the CMA sets its priorities when using its inspection and investigation powers.<sup>463</sup> This is similar to the FCA approach, whereby the issues warranting investigative action are chosen based on the FCA's priorities. Since the FCA adopts a risk-based approach that helps to identify risk, and devotes its resources accordingly, not all breaches of rules and principles will result in investigative action being taken, but when the breach amounts to a threat to its statutory objectives there must be an investigation.

It is worth mentioning that the FCA's setting of enforcement priorities leads to criticism that matters are unfairly selected for enforcement because they fall within a specified priority.<sup>464</sup> But regardless of this criticism, the prioritising can help the FCA to direct its powers and resources towards the investigation of important breaches, which can in turn help to protect the markets and consumers. The adoption of compliance and risk-based approaches will avoid wasteful use of CMA resources if absolutely *any* wrongful act is investigated. Pursuing every potential infringement takes up the CMA's power and time. These new approaches will allow it to focus on the most significant breaches and wrongful acts, enabling the enforcement tools and powers to serve their objectives and protect the markets.

The CMA can only use its power to uncover a breach of the CML and its Executive Bylaws. This has been criticised by scholars for limiting the CMA's investigative power to a narrow

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<sup>461</sup> This guidance for internal use at the CMA.

<sup>462</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>463</sup> *ibid.*

<sup>464</sup> Angela Hayes and Carlos Conceicao, *A Practitioner's Guide to Financial Service Investigation and Enforcement* (3<sup>rd</sup> edn, Sweet & Maxwell 2014) 152.

field.<sup>465</sup> It is important to highlight the weakness of limiting CMA investigation and inspection powers in this way: the CMA is the sole authority with the experience to capture the risks that face regulated firms, but it cannot consider any violation related to other laws, such as company law, because it is only responsible for reviewing and reporting violations of the CML and its Executive Bylaws. In practice, many firms rely on a CMA report that the business is complying with the law, whereas in reality it only complies with the CML and its Executive Bylaws. A CMA report can be used as evidence in court that a firm has clean records.<sup>466</sup> It is suggested that the CMA must not be limited to capturing violations of the CML, and its powers should be extended to cover any other law might affect the achievement of its objectives. This extension of CMA inspection and investigation scope will help to look at the big picture of a company's performance. The limited review of companies' performance without seeing the big picture was one of the causes of the 2008 crisis,<sup>467</sup> so giving the CMA sufficient power and scope to pursue its objectives is important to protect the markets.

Finally, the investigative powers exercised by the CMA staff are supported by the threat of punishment for non-compliance. There is a fine of 'not less than five thousand Dinars and not exceeding fifty thousand Dinars' if any person commits an action that may obstruct an investigation or any supervisory activity of the CMA or its employees, including if a firm/individual fails to enable a CMA employee to access any data or information deemed necessary by the CMA; if a firm/individual fails to comply with any final resolution issued by the Disciplinary Board (see below); or if a firm/individual provides the CMA with false or misleading information.<sup>468</sup> This punishment gives the investigator a strong and effective threat of sanction to force compliance by the regulated firm/individual.

## 2.1 Important comments

The enforcement of securities market regulation can be achieved through civil remedies and criminal sanctions, and market abuse enforcement varies between civil and criminal penalties.

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<sup>465</sup> Hussain Boarki, The legal protection for Capital Market Authority' Case study Kuwait and France, above (n 4) **Error! Bookmark not defined.** 233. See also Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 440.

<sup>466</sup> Participant No.3 stated that firms use the CMA's report to convince the judge that there is no misconduct behavior even through the report related to the CML and its Executive Bylaws only.

<sup>467</sup> Nikoletta Kallasidou, above, (n 249) 130.

<sup>468</sup> CML, Article 127.



Civil penalties include the imposition of monetary fines, and criminal law sanctions involve imprisonment or monetary fines.<sup>469</sup>

In Kuwait, administrative enforcement decisions are made by a body known as the Disciplinary Board, while in the UK system the equivalent entity is the Regulatory Decisions Committee (RDC). The Disciplinary Board is responsible for reviewing violations of the CML and its Executive Bylaws, as well as any complaints against KSE decisions. The law requires that any complaint against the KSE must be submitted within 15 days of the issuance of the decision.<sup>470</sup> Enforcement decisions related to KSE matters will be final.<sup>471</sup>

The Disciplinary Board has the authority to enforce administrative penalties on non-compliant firms and individuals and to refer violators (both firms and individuals) to the Capital Market Prosecutor, which can impose criminal sanctions. The mechanism for applying sanctions depends on the type of sanction being applied. The financial regulator should have at its disposal a wide range of sanctions and remedies, including monetary penalties.<sup>472</sup>

The composition of the Disciplinary Board in Kuwait gives some guarantee to alleged violators that they will be treated with fairness and impartiality. The Disciplinary Board must be chaired by a judge who is seconded by the Supreme Judicial Council,<sup>473</sup> and two members who are experts in financial and economic affairs should be present for the purpose of deciding administrative penalties for violations of the provisions of the law.<sup>474</sup> This stands in contrast to the UK equivalent, the RDC, which consists of a chairperson and several deputy chairs, but none of the members is from the judiciary. The chair of the RDC is a salaried employee of the FCA.<sup>475</sup> Furthermore, the FSMA and the Decision Procedure and Penalties Manual (DEPP – an FCA handbook) require that the chairs must be appointed by the FCA’s board on the recommendation of an independent group established for that purpose. The composition of Kuwait’s Disciplinary Board provides a form of trust and confidence in its decisions. A member of the Disciplinary Board is prohibited from having any direct or indirect interest in

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<sup>469</sup> Emiliós Avgouleas, *The Mechanics and Regulation of Market Abuse: A Legal and Economic Analysis*, (Oxford University Press 2005) 452.

<sup>470</sup> Bader AlMulla, above (n 62) 1011.

<sup>471</sup> CML. Article 140.

<sup>472</sup> Ana Carjaval and Jennifer Elliott, above, (n 424) 20.

<sup>473</sup> Note that in Kuwait, the Supreme Judicial Council is the body that is responsible for making recommendations to the Amir for all judicial appointments. It consists of Kuwaiti judges and Ministry of Justice Officials.

<sup>474</sup> Bader AlMullah, above, (n 62) 1009.

<sup>475</sup> Angela Hayes and Carlos Conceicao, above (n 464) 228.

any entity that is subject to the CML, nor may he/she be allied with any such entity during the time of his/her work on the board.<sup>476</sup> This prohibition is to ensure that the Disciplinary Board's members have no conflict of interest while carrying out their duties.

### **3. Investigative powers**

Gathering information is important in achieving the enforcement objectives, and proper data requests are part of an efficient enforcement regime. As the Hampton Principle states, 'Businesses should not have to give unnecessary information or give the same piece of information twice.'<sup>477</sup>

The CML gives the CMA a wide range of powers to request information and carry out inspections to achieve its objectives.<sup>478</sup> The CML aims to prevent insider trading by internal control procedures that firms must adopt to prevent misuse of inside information;<sup>479</sup> these controls are designed to detect the risks that come from a firm's activities. Thus investigative powers are used to ensure that firms' internal compliance procedures are in accordance with the best standards. The CMA team must investigate a firm's internal procedures using its latest transactions in the stock markets. If the investigation shows inconsistent or unusual trading in the firm's shares, the CMA focuses its resources on the share performance in the markets, which might lead to uncovering insider trading.

#### **3.1 Requests for information 'detection'**

The CMA has the power to request any licensed person<sup>480</sup> to provide any information or documents in pursuit of its objectives. It may also request other supervisory authorities to submit any documents that may be related to a particular firm or individual.<sup>481</sup> For example, the CMA can ask any public authority if it has an agreement with a listed company to prevent the use of inside information, and oblige the company to disclosure material information. The CMA also has the power to request information in relation to an unauthorised firm engaging in securities activities.<sup>482</sup> For example, the CMA can ask a bank regulated only by the CBK to

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<sup>476</sup> CML, Article 141.

<sup>477</sup> Philip Hampton, 'Reducing Administrative Burdens: Effective Inspection and Enforcement: Final Report' (March 2005) HM Treasury, London.

<sup>478</sup> The Executive Bylaws, Module Three, Chapter One, Article 2-1.

<sup>479</sup> CML, Article 66.

<sup>480</sup> According to the CML, the term 'persons' include firms and individuals.

<sup>481</sup> The Executive Bylaws, Module Three, Chapter One, Article 1-1.

<sup>482</sup> CML, Article 5.

provide information about a listed company's proposal to ask for a loan for a merger. The CMA has the power to request information not only from registered persons but also non-registered persons practising securities activities.<sup>483</sup> This extension of CMA enforcement powers to engage with non-registered persons who are dealing with securities is a promising development,<sup>484</sup> and helps to ensure that the CMA can protect the markets from any misconduct. It complies with the IOSCO Principles recommending that the regulator should have a wide range of powers to request information.<sup>485</sup>

Another important feature in the Kuwait enforcement regime is that the CMA can seek information or request documents by telephone, at a meeting or in writing.<sup>486</sup> This is helpful, and serves the CMA's objective of using technology to communicate with the market.<sup>487</sup> Furthermore, the CMA has the power to request any firms or persons to submit immediately any information or explanation related to achieving the disclosure and transparency objectives.<sup>488</sup> Thus the CMA has wide powers to gather information in the financial sector.

In the UK system, the FCA and the PRA have broad powers to request information, including information from regulated persons and those who do not need or do not have authorisation under Part 4A of the FSMA to carry out their business.<sup>489</sup> The FCA is given the power to gather information under sections 97, 131E, 131EA, 165–169 and 284 of the Financial Services Act 2012,<sup>490</sup> and may use its power under s. 165 of the FSMA to request information from authorised entities. Both regulators share the same powers to require information, but the FCA may appoint a skilled person to collect information (FSMA, s. 166), while there is no provision in Kuwait's approach regarding a skilled person. An additional power of the UK authorities (FSMA, s. 165A) is to obtain disclosure of information that is or might be relevant to the stability of any aspect of the UK financial regime.<sup>491</sup> These powers are likely to be useful in

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<sup>483</sup> The Executive Bylaws, Module Three, Chapter Two, Article 1-1.

<sup>484</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>485</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> accessed 27 January 2020

<sup>486</sup> Hussain Boarki, 'The legal protection for Capital Market Authority' Case study Kuwait and France, above (n 4) 337.

<sup>487</sup> In Kuwait, most of public service authority do not use technology in their daily work such as emails.

<sup>488</sup> The Executive Bylaws, Module Ten, Chapter One, Article 1-2-1

<sup>489</sup> Angela Hayes and Carlos Conceicao, above (n 464) 31.

<sup>490</sup> The FCA Enforcement Guide (1/4/2014) s.3.1

<sup>491</sup> FSMA, s 165A(3).

protecting the integrity of the markets and safeguarding consumers. The FCA's wide-ranging power is similar to the CMA's power in Kuwait.

In addition, in the UK Principle 11 of the 'Principles for business' set forth in the FCA Handbook<sup>492</sup> is specifically relevant to regulated firms, while Principle 4 of the 'Statement of principles for approved persons' applies to 'approved persons'.<sup>493</sup> Note that Principle 11 covers unregulated activities by regulated firms or individuals, which must comply with Principles 4 and 11 whether or not the relevant regulator has been given notice of the activities.<sup>494</sup> The enforcement guidance states that the regulator normally expects to give reasonable notice of a visit, but on rare occasions it may access premises without notice.<sup>495</sup> The possibility of an unannounced visit is 'intended to encourage firms to comply with the requirements and standards under the regulatory system at all times'.<sup>496</sup>

In both systems the financial regulators have the power to request information and ensure that an authorised person complies, but in Kuwait's system the regulator goes even further to cover unauthorised persons dealing with securities activities. This power must be limited to the activities that the unauthorised person is carrying out, according to CML Article 5.<sup>497</sup> There was debate about the CMA's authority over unauthorised persons:<sup>498</sup> it is the researcher's opinion that it is good practice for the CML to give the CMA the authority to request information from an unauthorised person. It is important to ensure compliance with the law, whether as an authorised person or not, as the ultimate goal is to protect the markets. It is worthwhile to mention that in the UK system unauthorised firms and individuals are under no obligation to comply with requests for information because they are not specifically mentioned

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<sup>492</sup> Financial Conduct Authority, *FCA Handbook* <<https://www.handbook.fca.org.uk/handbook>> (accessed 19 February 2018) [hereinafter FCA Handbook]. PRIN 2.1.1 contains the 11 principles. Principle 11 states: 'A *firm* must deal with regulators in an open and honest way, and must disclose to the FCA appropriately anything that relating to the *firm* of which that regulator would reasonably expect notice.'

<sup>493</sup> Statements of Principle and Code of Practice for Approved Persons, February 2018 <<https://www.handbook.fca.org.uk/handbook/APER.pdf>> (accessed 13 March 2020). Chapter 1.1A sets forth the scope of application.

<sup>494</sup> Angela Hayes and Carlos Conceicao, above (n 464) 36.

<sup>495</sup> SUP 2.3.2 G and SUP 2.3.6 G, *FCA Handbook*.

<sup>496</sup> SUP 2.3.2 G.

<sup>497</sup> Hussain Boarki, 'The legal protection for Capital Market Authority' Case study Kuwait and France above (n 4**Error! Bookmark not defined.**) 336.

<sup>498</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 540. See also Hussain Boarki, 'The legal protection for Capital Market Authority' Case study Kuwait and France, above (n 4**Error! Bookmark not defined.**) 477.

in Principle 11.<sup>499</sup> However, it is unlikely that a firm would refuse to comply with a voluntary request on that basis: an unauthorised firm usually cooperates with a request for information to assure the regulators that its suspicions are unfounded and avoid a formal investigation.<sup>500</sup> In that sense, the Kuwaiti regulator is in a stronger position because the CML includes a clear provision that unauthorised persons who deal in securities activities will be subject to CMA enforcement power; this is in keeping with its overall emphasis, which is to enhance trust and confidence in the markets.

It seems that the CMA has sufficient powers to gather information, but the question is how the collected data are analysed. There is no stated mechanism to analyse the information gathered and set priorities accordingly. Some information is neglected, and there is no expertise to analyse data and reach results about a given company. This is serious weakness that needs to be highlighted and reformed to improve supervision of financial services and stock markets. Qualified staff and experts are needed to analyse and assess information in order to supervise the highest-risk firms.

When the researcher asked the interviewees for their opinion of ‘the effectiveness of the CMA’s power to request information in the markets, and if it gives the CMA a clear picture about a firm’s activities to uncover breaches and crimes in the markets’, six of them said that the CMA has a wide range of powers to seek information, but there is lack of expertise among CMA staff to analyse the data and uncover risk and crisis.

Participant No. 1:

There is understanding about the importance of the CMA staff reviewing the company’s record and their judicial power to request any information or record. The CMA staff needs time to improve their skills and address the violations.

Participant No. 2:

The CMA must enhance their role to check the accuracy of the disclosed information by requesting information or sending an inspector to visit the listed company to examine the information. In fact, the CMA found out that some companies announced that they are in the process of a merger when in reality there was nothing in this regard. Therefore, the CMA’s power to seek information is

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<sup>499</sup> Angela Hayes and Carlos Conceicao, above (n 464) 36.

<sup>500</sup> *ibid.* 37.

wide and sufficient but the staff must have the appropriate skills to uncover the violation.

Participant No. 3:

In general, insider dealing is a crime that rarely happens in stock markets. In order to discover it, the CMA should have sufficient tools and qualified staff to uncover financial crimes. The current tools are sufficient to gather information and the team is qualified but needs experience to ask the right questions to uncover the crime.

Participant No. 4:

The CML grants the CMA sufficient tools and power to seek information but the CMA staff needs some training and improvement.

Participant No. 5:

I personally believe that one of the strong powers that the CMA has is their investigation power to seek information. Their powers are wide and provide the required tools, but the staff must work harder to use their power correctly.

Participant No. 6:

We have not faced any problem with the CMA's power to request information. Listed companies comply with any request to provide information, otherwise they will face punishment. Therefore, the power exists but the CMA should ask the right questions and/or request the important information.

### 3.2 Periodic reports

The CMA has power to require the submission of periodic reports or documents outside an investigation. It is compulsory to provide an item of information if the law clearly states that an authorised person is required to submit particular reports or documents. Such reports include details of internal corporate procedures required by the CML to prevent insider trading.<sup>501</sup> Listed companies must present a report of all suspicion transactions and any misuse of information or leaks in stock markets. If the authorised person does not comply with this request it may be subject to sanctions. It is essential to ensure that the data requests are based on a risk-based approach so firms are not asked to provide information without purpose (in line

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<sup>501</sup> The Executive Bylaws, Module Fifteen Chapter Seven, Article 7-3.

with the Hampton Principle<sup>502</sup>). This helps to reduce the administrative burden and improve the effective use of the information.

Furthermore, there is specific information that licensed and unlicensed persons are required to submit to the CMA because the information or report might affect the stability of the economy.<sup>503</sup> This helps to ensure that regulated firms comply with the CML and generates alerts for certain issues to reinforce public trust in the stock markets. Additionally, the data are required to assess risks and apply the risk-based approach. The CML provides a well-documented reporting regime, but the CMA needs guidance to ensure that regulated firms understand the purpose of providing this information. There is no published CMA policy regarding its strategy to enforce the law. Even the CMA inspection guidance is not published, and information about the CMA's policy is not in the public domain.<sup>504</sup> There is vague and unclear policy regarding data collection, and no mention of a risk-based approach as a policy. It is not clear how the CMA uses the information collected from listed companies.

The CML has 16 modules which describe its Executive Bylaws in detail, and each module has provisions related to data collection.<sup>505</sup> Three modules specifically concern collecting data, whether annually or otherwise, regarding securities activities and registered persons, policies and procedures of licensed persons, and disclosure and transparency. Although all the required information is important to financial services and stock markets, it is complex to follow and difficult to understand.<sup>506</sup> The accessibility of regulation is very important to ensure its application, and it needs guidance and explanation to ensure all information has a purpose. Hence the CMA needs to publish its policy on collecting data.

In the UK the FCA obtains information related to an internal investigation or report from an external law firm, which could help if enforcement action is anticipated.<sup>507</sup> This attitude is a result of using a compliance approach that encourages firms to disclose any violation of the

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<sup>502</sup> Philip Hampton, 'Reducing Administrative Burdens: Effective Inspection and Enforcement: Final Report' (March 2005) HM Treasury, London.

<sup>503</sup> Hassan AlEsady, 'The Impact of a Country's Financial, Economic, and Political Risk on the its Creditworthiness and Stock Market Development: Cross Sectional Analysis' (2009) 16 Arab Journal of Administrative Sciences 343, 348, 380.

<sup>504</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>505</sup> The Executive Bylaws.

<sup>506</sup> Participants Nos 1 and 6 stated that the current structure of the law make it harder for anyone to review the law and understand it.

<sup>507</sup> The FCA Enforcement Guide 3.1.2.

law voluntarily, or report to help the FCA to enforce the law. One of the major reforms after the financial crisis is expanding reporting to the FCA through public disclosure.<sup>508</sup>

#### 4. Inspection

Inspection is another way to gain information about non-compliant behaviour. Administrative inspection includes on-site inspectors with access to firms' records and files.<sup>509</sup> The CMA has two types of inspectors: those with normal powers to investigate and gather information by requesting it from a company; and those with judicial power who may access and review a company's records without permission from the prosecutor if the inspector suspects crimes such as insider trading. Judicial powers are extraordinary powers, as explained below.

Generally, an inspection does not aim to discover a specific crime; the objective is to have an overall review to ensure that the firm is following the law.<sup>510</sup> There are two kinds of inspection: the first covers all the firm's operations and transactions, while the second type is designed to inspect a specific transaction.<sup>511</sup> On-site inspection focuses on analysing the challenges and risks that a firm faces to ensure that it can undertake financial activities and prevent any crime in stock markets.<sup>512</sup>

The Hampton Principle states: 'No inspection should take place without a reason.'<sup>513</sup> The CMA's resources must be targeted on inspecting the highest-risks firms as established by risk assessments, so these firms should receive many more inspection visits than medium-risk firms. The CMA has the authority to perform periodical inspections with prior notice, and can also perform inspections without prior notice to achieve its objectives, as stated in the CML

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<sup>508</sup> Mads Andenas, and Iris Chiu. *The foundations and future of financial regulation: Governance for responsibility*. (Routledge, 2013). 418.

<sup>509</sup> CMA, Article 5(4): 'The Authority shall carry out all the work necessary to achieve its goals...(4) Conduct inspections, and supervise Securities dealings and the activities of the Licensed Persons in accordance with this Law.'

<sup>510</sup> Mubarak AlNwabeat, *An Explanation of General Principles for Criminal Court Procedures*, (1<sup>st</sup> edn, no publisher, 1998) 250. See also The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>511</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>512</sup> The CMA Report for the Financial Year 2016/2017 (in Arabic)

<[>](https://www.cma.gov.kw/ar/web/cma/pdf-viewer?file=/documents/20622/87708/6th+Annual+Report.pdf/94100eca-817f-44d1-8309-e83aa8af3cbd#page=1&zoom=page-fit,-22,849) accessed 23 November 2017 [hereinafter The CMA Financial Report 2016/2017].

<sup>513</sup> Philip Hampton, 'Reducing Administrative Burdens: Effective Inspection and Enforcement: Final Report' (March 2005) HM Treasury, London.



and its bylaws, or to investigate complaints and reports submitted to the CMA.<sup>514</sup> The latter inspections are carried out by staff who have judicial power (explained below) and can access the records and data of licensed persons.<sup>515</sup> There is an argument that an inspection without prior notice must be limited to investigate only complaints or reports that have been submitted to the CMA.<sup>516</sup> This limitation could be considered as a constraint on the inspection powers.<sup>517</sup> However, in practice, the CMA can inspect any licensed persons if it considers this necessary to achieve the CML objectives, although that interpretation could be potentially challenged in court. The stated provision, ‘to achieve the CML objectives’, gives the CMA wide discretionary power that it may wield in relation to regulated firms and individuals, which could to some extent be considered as inspection without prior notice. Any inspection or investigation can be ‘to achieve the CML objectives’, which provides the CMA with wide powers to conduct inspections. In a rule-based system like that in Kuwait, regulation must be clear and enforceable, hence the interpretation of ‘to achieve the CML objectives’ should be more precise. It is therefore suggested that the CMA should provide examples and clear interpretation of using inspection powers to achieve the CML objectives.

With regard to on-site inspections, the CMA has the authority to visit regulated firms and inspect their records and books.<sup>518</sup> There is a regular routine inspection for certain purposes, and other inspections without determination. In addition, there is the aforementioned power to inspect without giving prior notice. On-site inspection is an essential tool that the CMA uses to uncover insider trading.<sup>519</sup> Having the ability to request information and documents from a firm suspected of insider trading is essential to achieve strong stock markets.<sup>520</sup> In the fiscal

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<sup>514</sup> Executive Bylaws, Module Three, Chapter Two, and Article 2-2 which provides as follows: ‘The Authority shall perform periodical inspection after prior notice to ensure compliance with provisions of the Law and these Bylaws, and applicable policies and procedures. It may inspect without prior notice in order to achieve its objectives stated in the Law and these Bylaws or to investigate complaints and reports submitted to it’: <https://www.cma.gov.kw/pdfviewer/?file=/documents/20622/487166/E03-+Enforcement+of+the+Law.pdf/35e25c4a-688a-4370-9583-1e77cf2ecb81#page=1&zoom=page-fit>, -22,849 accessed 19 February 2020. See also The CMA, ‘Guidance on The CMA’s Internal Inspection’ (unpublished June 2019).

<sup>515</sup> CML, Article 30.

<sup>516</sup> Hussain Boarki, ‘The legal protection for Capital Market Authority’ Case study Kuwait and France, above (n 4) 404

<sup>517</sup> Ibid.

<sup>518</sup> Executive Bylaws, Module Three, Chapter Two, Articles 2-2 and 2-3., see also The CMA, ‘Guidance on The CMA’s Internal Inspection’ (unpublished June 2019).

<sup>519</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 15 January 2019 28 January 2020. 16

<sup>520</sup> Bernard Black, ‘The Core Institutions That Support Strong Securities Markets’ above (n 12) 1567, 1571.

year 2016/2017 there were 11 inspections of investment firms and 13 inspections of funds. Regarding inspections with a determined purpose, there were 32 inspections of firms, auditors and intermediaries.<sup>521</sup>

Before issuing the final report detailing the outcome of an on-site inspection, the CMA can give the regulated entity the opportunity to reform or explain its situation.<sup>522</sup> This opportunity is based on CMA discretion, which raises a concern about fairness and justice. The various steps in the process of inspection and reporting are summarised here. First, the on-site inspection involves collecting all relevant information and making observations;<sup>523</sup> these are used to prepare an initial report. Secondly, the initial report is sent to the regulated person(s), so it has the opportunity to respond and comment on what the inspection team observed.<sup>524</sup> The regulated person has ten business days from the date of receiving the initial report to respond.<sup>525</sup> Thirdly, after a discussion based on the initial report with the inspected person, in some cases the firm has an opportunity to correct the observations within a period of time set by the CMA.<sup>526</sup> This procedure is optional for the CMA to give a non-compliant firm the chance to correct the situation. There is no policy, so the CMA uses this power randomly. The last step in this process is for the CMA to prepare the final report, which sets out the results of the inspection.<sup>527</sup> This final report may include the CMA initiating disciplinary procedures to correct violations identified in the report.<sup>528</sup>

It should be noted that this procedure gives the regulated person the chance to correct all the actions or transactions that were observed to be non-compliant with regulations. This is an application of the CMA's compliance approach to persuade companies to comply with the law.<sup>529</sup> The regulated person may have the opportunity to correct its position before the issue of the final report: this procedure is optional and exercised at the discretion of the CMA. For example, sometimes the CMA will issue the final report without first discussing the issues with the inspected person and allowing it to comment. Thus the CMA may start disciplinary

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<sup>521</sup> The CMA Financial Report 2016/2017

<sup>522</sup> Executive Bylaw, Module Three, Chapter Two, Article 2-3., see also The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>523</sup> Executive Bylaws, Module Three, Chapter Two, Article 2-3(1).

<sup>524</sup> *ibid.*, Article 2-3(2).

<sup>525</sup> *ibid.* Article 2-3(2).

<sup>526</sup> *ibid.* Article 2-3(3).

<sup>527</sup> *ibid.* Article 2-3(4).

<sup>528</sup> *ibid.* Article 2-3(4).

<sup>529</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

procedures without any prior consultation. In such a case, the inspected person will miss the chance to correct its actions and potentially avoid disciplinary procedures. To treat all inspected persons fairly, it is suggested that this provision should be amended to give all inspected persons the opportunity to respond and comment on the initial report. This would ensure that all licensed persons are treated equally, with fairness and justice, which ultimately will better serve the CMA's objective of protecting the market's integrity.

The CMA has the authority to supervise and inspect a third party if that party is related in some way to securities activities, in accordance with CML Article 5. The CMA can supervise, inspect, investigate and request information from a third party. The third party cannot ignore the CMA's request and is obliged to answer the questions, otherwise it will be subject to civil sanctions according to CML Article 127. If the third party is not registered as an approved person and not related to securities activities, the CMA cannot require the party to make changes or improvements. For example, auditing firms which are licensed by the MOCI cannot be supervised or inspected by the CMA.<sup>530</sup> The only authority that can supervise and inspect is the authority providing the licence – the MOCI.<sup>531</sup>

From a risk-based approach perspective, the CMA should adopt a policy of using on-site and off-site inspection to allocate its resources to the firms presenting the greatest risks to its regulatory objectives.<sup>532</sup> The risk-based approach works by identifying the relevant risks and measuring and assessing their impact on CMA objectives. It also evaluates regulated firms' internal risk management systems to control and mitigate these risks. The risk assessment result will determine the regulator's prioritisation of its resources, paying most attention to the highest risks to its objectives. It provides an enforcement plan to manage the time and number of on-site or off-site visits to regulated firms. It is a huge development for the CMA to adopt a risk-based approach to using its inspection powers wisely.<sup>533</sup>

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<sup>530</sup> Kuwait Law No. 5 of 1981 Regarding the Practicing in the Auditing Profession

<sup>531</sup> Hussain Boarki, 'The legal protection for Capital Market Authority' Case study Kuwait and France above (n 4) 338

<sup>532</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) 19 available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>>> accessed 12 February 2020.

<sup>533</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

In the UK the FCA has the power under FSMA s. 165 to require information and documents to support both its supervisory and its enforcement functions.<sup>534</sup> In accordance with s. 165, the FCA and PRA have investigatory powers to serve a written notice on an authorised person to provide specific information and documents within a reasonable period. The investigatory power's scope of application is very wide. The FCA can send an enforcement notice to require a person to produce information; this can be sent not only to an authorised person, but also to any party related to an authorised person. Connected parties include persons who are – or at a relevant time have been – members of the same group, controllers of the firm, officers, managers, employees or agents.<sup>535</sup> This provision is broader than the Kuwaiti provision, which includes third parties but only those that had a direct relation to the relevant events.<sup>536</sup> This condition of only involving third parties who are directly related to the events is presumably meant to protect the privacy of the third party.<sup>537</sup> It should be noted that most cases, whether in Kuwait or in the UK, relate to commercial matters and the reputation of third parties is important. Thus it is good practice to set forth conditions that must be fulfilled before involving third parties in inspections or investigations.

#### 4.1 Judicial power

In general, there are only limited situations where it would be legitimate for an authorised firm to withhold requested material. However, the CML gives CMA inspectors an unusual power called 'judicial power'. This allows selected inspectors who have reasonable suspicions of a crime violating the CML and its Executive Bylaws to verify the evidence and inspect and review a firm's documents and records, including confidential data.<sup>538</sup> If the CMA is carrying out an on-site inspection and the judicial officer discovers a violation of the law, he or she can inspect further and ask the firm for certain documents; the firm cannot refuse to provide them.<sup>539</sup> The judicial officer has the power to inspect suspicious transactions or behaviour by a regulated firm; this power is so wide-ranging that only a few CMA staff are given a judicial remit. Conducting these inspections helps to identify errors and non-compliant behaviour at an early stage to uncover fake disclosure or insider trading. It helps to reveal any non-public

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<sup>534</sup> Angela Hayes and Carlos Conceicao, above (n 464) 38.

<sup>535</sup> FSMA, s 165(7) (a) and s 165(11), which defines a 'connected person' for the purpose of this section.

<sup>536</sup> CML, Article 5.

<sup>537</sup> CML, Article 142.

<sup>538</sup> CML, Article 30.

<sup>539</sup> CML, Article 30 and the Executive Bylaws, Module Three, Chapter Two, Articles 2-4 and 2-5.

information that might lead to insider trading on stock markets. This is the most powerful tool for CMA staff, and if they use it properly they will succeed in preventing any leak of inside information. It must be noted that these extraordinary judicial powers are related to discovering crimes such as insider trading or market manipulation, and not to any civil violation of the CML; the crime must be stated in the CML and its Executive Bylaws, rather than being a corporate crime or misuse of power stated in deferent law.

It worth mentioning that the CMA annual reports do not state how many crimes have been discovered by judicial officers, and even the referral reports do not state that a crime has been discovered by such an officer.<sup>540</sup> Although judicial power gives a wide-ranging ability to collect and gather information, it is difficult to evaluate this power without reports of how many crimes have been uncovered by judicial officers. The lack of information in the annual reports and CMA website is an obstacle to evaluating the effectiveness of judicial power in discovering crime in financial services and stock markets.

The qualifications and training of judicial officers are an issue that impacts on the effectiveness of their investigations. The judicial officer must be well trained to discover sophisticated crimes such as insider trading. The interviews (see below) confirmed a lack of experience and training to prepare judicial officers. Participant No. 2 highlighted that judicial officers do not uncover many crimes in stock markets due to their lack of experience.

Another important element revealed by the interviews is the unclear limits of the judicial officer's power. Judicial powers are wide, and there is no clarification or guidance to train officers in how to use them. Participants Nos 1 and 5 said there would be new guidance to fill this gap, set limitations and explain judicial power more clearly. The internal inspection guidance was issued in June 2019,<sup>541</sup> with an explanation of the CMA's policy of adopting a risk-based approach as a basis to prepare investigation plans. It is the first time on record that the CMA has adopted a clear policy on investigation.<sup>542</sup> Although the guidance includes much information about CMA policy and inspection power, there is no provision about the

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<sup>540</sup> The CMA annual report 2018/2019 available at <<https://www.cma.gov.kw/ar/web/cma/annual-reports>> accessed 18 March 2020.

<sup>541</sup> After the researcher completed the fieldwork in May 2019.

<sup>542</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

limitations of judicial officers' powers. In addition, this guidance has not been published – it is classified document, and only CMA staff can see it.

In terms of the validity of judicial officers' findings for use as evidence in court, if a violation is proven by a judicial officer the investigation outcome can be used in court as valid evidence to punish the non-compliant firm. The firm cannot argue in court that this evidence was obtained without the prosecutor's permission, because judicial officers have the authority to write a report about actions committed in violation of the CML that can be used as evidence. This power can also be used in response to a particular enquiry that has been submitted to the CMA. The judicial officers have subpoena power to call witnesses to complete their investigation.<sup>543</sup> This is an exceptional power which gives the CMA the authority to inspect without first obtaining the prosecutor's permission. Such permission, which is required by other laws, exists to ensure that private property is always protected from abuse of power by an administrative entity – such as the CMA. Hence some scholars insist that CMA staff must not have judicial power; instead, they argue that the staff must be under the prosecutor's jurisdiction if they wish to carry out inspections.<sup>544</sup> Although this argument is well intentioned, commercial matters and economy stability need quick action and the proper tools to discover crimes, without any of the delays that would be inherent in first seeking prosecutorial permission. In fact, the broad CMA power to investigate and gather information is a good basis for strong stock markets and protecting market integrity from insider trading.<sup>545</sup> It serves the regulator's objectives to provide sound regulatory supervision to protect the marketplace and its participants.

#### 4.1.1 Confidentiality

It is important to note that no person can refuse to provide documents or information required by judicial officers on the basis of the confidentiality of such information or documents, or on the basis of a superior's instructions not to disclose them.<sup>546</sup> This means that all firms and individuals must not refuse the judicial officers' requests, even if those requests are related to confidential matters. It should be noted that providing the CMA with large powers to obtain

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<sup>543</sup> Executive Bylaws, Module Three, Chapter Two, Articles 2-5.

<sup>544</sup> Jalal S Othman, *Commentary on Law No.7 of 2010 regarding the Capital Market Authority and Organizing the Securities Activities and its New Executive bylaws* (Dar Al Eqraa, 2016) 962.

<sup>545</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 15 January 2019 28 January 2020. 16

<sup>546</sup> Executive Bylaws, Module Three, Chapter Two, Article 2-7.

information and documents is suggested in the IOSCO standards to ensure the regulator has sufficient information to enforce the law.<sup>547</sup> It helps the CMA to exercise its power if it has wide information to protect the markets, but this power affects the rights to confidentiality for regulated firms, which is one of the standards that IOSCO also adopts.<sup>548</sup>

This stands in contrast to the UK approach, which includes limited circumstances in which it would be acceptable for an authorised person to withhold requested material – for example, if the person is being investigated.<sup>549</sup> Furthermore, based on confidentiality, the authorised person can refuse to provide information. There are certain laws and circumstances that the FCA takes into consideration to protect confidentiality, such as banking confidentiality, legal privilege and the Data Protection Act 1998. All these protections of confidentiality in principle should be considered by the Kuwait legislature, with a view to amending the current provisions to ensure the protection of rights to confidentiality. Furthermore, when the FCA uses its search and seizure powers the action must be based on a warrant to enter the premises of a regulated firm to obtain documents or information.<sup>550</sup> Even if the circumstances are urgent, there is need to obtain a warrant to seize any documents or records.

To evaluate the effectiveness of the judicial power held by some CMA staff, the researcher asked the interviewees: ‘Is the judicial officer’s power to seek information sufficient and does it help to discover crimes in financial services and stock markets?’ The seven experts confirmed that judicial power is a great development for the CMA, but the lack of officer experience and uncertain limitations of the power must be reconsidered.

Participant No. 1:

Judicial power is a unique power that some of the CMA’s staff have to seek information or request documents to uncover crimes. The confidentiality of information and the limitation of their power are always under consideration of the CMA. We can say that the judicial officer needs some time to improve his/her skills. By the way, soon the CMA will issue a new inspection guidance, which will clarify the inspection’s limitation.

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<sup>547</sup> Principle 3 of IOSCO, ‘Objectives and Principles of Securities Regulation’, June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 18 March 2020.

<sup>548</sup> Principle 5 of IOSCO, ‘Objectives and Principles of Securities Regulation’, June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 11 March 2020.

<sup>549</sup> Angela Hayes and Carlos Conceicao, above (n 464) 40.

<sup>550</sup> FSMA, s 176

Participant No. 2:

There were some incidents where the judicial officer overstepped his role and privileges as an inspector and he personally opened some files and records. The CMA issued 'on-site inspector guidance' to ensure that the inspector and judicial officer know their limits. There is no doubt that the judicial power is great and provides a sufficient tool to uncover crimes. Again, the issue with inexperienced inspectors to uncover the crime is there. Most judicial officers' violation reports are about listed companies not providing the officer with information or records, but none about discovering financial crimes. It is difficult for the officer to conclude that there is a violation of the law without doing a proper and skilled investigation. To be honest, the market has been developed and listed companies are aware of the importance to obey the CMA law and its bylaws but some listed companies intentionally breach the law, therefore, the CMA must increase its inspections to capture any illegal activities. The Enforcement Department must increase their role involving more unexpected visits and improve their skills.

Participant No. 3:

Judicial authority is an important power for an inspector in the financial sector, but the critical issue is the limitations of the judicial officer in fieldwork. For example, the inspector might reveal confidential information regarding the profession of a company that is not under the CMA's supervision, such as an oil company, which had confidential information. Therefore, it is necessary that there is clear idea about the limitations of the inspector.

Participant No. 4:

The CMA's Inspector team does not have enough experience to inspect and investigate new companies, like professional companies such as auditing. The law added a new entity such as professional companies that the inspector team does not know how to inspect their books and files or what they should look for. This is in addition to the judicial officer having unlimited power to request any information or files. The purpose of the law must be stated to ensure that the inspector serves the objectives of the law. The authority of the inspector, especially one who has judiciary power, gives unlimited power to request any information or files. This unlimited power must be organised and monitored to protect companies that are not under the supervision of the CMA. The purpose of law must be stated to ensure that the inspector serve the objectives of the law.

Participant No. 5:

The judicial powers are the beauty of the CMA powers to seek information. Their weaknesses are lack of expertise and unclear limitation, which will be improved by inspection guidance.

Participants Nos 6 and 7 stated they had no experience or knowledge about judicial powers in the field.



## 5. Investigation outcome

The investigator's decision on a matter depends on the seriousness of the violation and the evidence collected that can prove the crime or violation. There are two types of procedures: criminal and administrative. The outcome of an investigation may result in administrative<sup>551</sup> rather than criminal sanctions<sup>552</sup> for crimes such as fake or incorrect disclosure. If the investigation reveals evidence that a crime such as insider dealing has been committed, the investigator refers the case to the CMA prosecutor to proceed with criminal procedures in a court.<sup>553</sup> This research did not investigate court sanctions, but only examines the CMA enforcement decision. It is vital to highlight that the CMA has the power to settle a criminal case before the courts reach a final judgment: this is an important tool that the CMA uses to punish non-compliant firms that commit crimes.

If an investigation reveals evidence that a violation has been committed, the investigator prepares a report to the CMA Board of Commissioners; this may contain a recommendation to refer the suspect to the Disciplinary Board.<sup>554</sup> In the Kuwaiti approach the investigator's report is not provided to the accused, but remains in the CMA's records. This is slightly different from the equivalent process in the UK, whereby the FCA formulates a letter with its preliminary findings, and in some circumstances the accused may be able to obtain a copy of the letter in an urgent case.<sup>555</sup> In Kuwait the suspected person is only informed of the investigator's decision, without any detail.<sup>556</sup> There is a lack of transparency in terms of investigation outcomes: the public and suspected persons should have access to investigation reports to ensure there is consistency in investigation procedures. It also provides guidance and helps awareness if the public understand the thematic pattern of the investigation process.

It is worth mentioning that there is an unclear legal framework for the CMA to proceed with criminal and administrative procedures. For example, in January 2018 the CMA lost a case against an investment firm that was charged with fictitious trading: the law does not provide any clear definition of 'fictitious trading' and there is no interpretative guideline as to how to

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<sup>551</sup> Executive Bylaws, Module Three, Chapter Four, Article 4-13.

<sup>552</sup> Executive Bylaws, Module Three, Chapter Six, Article 6-1.

<sup>553</sup> Ibid.

<sup>554</sup> Executive Bylaws, Module Three, Chapter Four, Article 4-13.

<sup>555</sup> Angela Hayes and Carlos Conceicao, above (n 464) 176.

<sup>556</sup> Executive Bylaws, Module Three, Chapter Four, Article 4-14, Executive Bylaw, Module Three, Chapter Six, Article 6-1.

apply the appropriate penalties or refer the case to the prosecutor. The firm was successful in proving that it had not engaged in fictitious trading.<sup>557</sup> It is important to give some assistance in interpreting the articles of financial regulation: it is difficult to apply all the rules and regulations without a clear framework and guidance for interpretation. This would also help the regulator and judges to protect the markets by imposing the appropriate penalties.

The Board of Commissioners may refer a suspected person to the Disciplinary Board or issue a warning to the suspect to cease committing violations.<sup>558</sup> It may require an undertaking not to repeat such a violation in the future, and may impose additional supervision on the violator.<sup>559</sup> If the CMA Board of Commissioners refers the matter to the Disciplinary Board for an enforcement decision, the Disciplinary Board issues a decision about the referred violation.<sup>560</sup> The Board of Commissioners and relevant parties are notified of the Disciplinary Board's decision within seven business days of its date of issue.<sup>561</sup> On the other hand, if the investigation is deemed not justified the suspect person is notified of the decision and can obtain a certificate confirming the result from the CMA.<sup>562</sup>

Having outlined the various possibilities regarding an investigation's outcome, there are some finer points that are worth noting.

First, the Board of Commissioners is the authority responsible for deciding whether or not to refer a suspected violator to the Disciplinary Board; that decision is based on the investigator's report, which is wrapped in secrecy..<sup>563</sup> The CMA cannot refer the suspected violator without the investigator's report; this ensures that the suspect is afforded his/her full rights to defend himself/herself. The investigation finding is for CMA use only, and the suspected violator does not have a chance to review it. O Principle 4 of the IOSCO is to ensure that the investigation process is clear and just,<sup>564</sup> so to comply with this the CMA should share the investigator's report with the suspected violator to give them a chance to comment on the findings. In the UK, in contrast, in the recent judgment on *Macris* against the FCA the court confirmed that

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<sup>557</sup> Case No. 25/2014 First Instance Court, Appeal Court Case No. 14/2017.

<sup>558</sup> Executive Bylaws, Module Three, Chapter Four, Article 4-13.

<sup>559</sup> CML, Article 143.

<sup>560</sup> Executive Bylaws, Module Three, Chapter Four, Article 4-13(2).

<sup>561</sup> *ibid.* Article 4-13(3).

<sup>562</sup> *ibid.* Article 4-14.

<sup>563</sup> *ibid.* Article 4-13.

<sup>564</sup> IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 24 January 2020

publication of investigation findings is in the public interest, which means it is important not only for the suspected violator but also for the public.<sup>565</sup> The FCA not only discloses the investigation finding to the suspected violator but also publishes it on the FCA website to enhance transparency in the markets. This gives a chance to the suspected violator to review the investigator's finding and comment on it.

Furthermore, the FCA sends a preliminary finding letter to a suspected violator before referring the matter to the RDC. In general the suspect will have a chance to review the letter and comment, but there are exceptional circumstances where the FCA may not send the letter to the suspected violator. (These exceptional circumstances are not detailed here, as they are not subject to analysis in this study.) This practice of sending the letter to a suspect for comment is useful, because it provides better-quality and more efficient decisions. The response to this letter should be submitted to the FCA within a reasonable period, normally 28 days.<sup>566</sup> This practice is an application of IOSCO standards: the regulator should provide information about the decision and decision-making processes.

Secondly, there is significant discretionary power in the CMA's decision either to refer the suspected violator to the Disciplinary Board or to issue a warning letter requiring a pledge not to repeat the violation. There is no requirement for the CMA to issue a warning letter; the decision on how to proceed falls solely within the CMA's discretion. This may lead to inconsistencies in handling suspected violators. Not publishing the investigation findings means no guidance is provided to other regulated firms to be aware of the thematic pattern the CMA follows. The investigation findings must be published to give guidance for future behaviour.<sup>567</sup> There should also be a list of all the violations that result in a warning letter rather than referral to the Disciplinary Board, plus some conditions or criteria to guide the CMA when deciding whether to refer a case or issue a warning. For instance, if it is a first offence or the violation did not harm a third party, a warning letter would normally suffice. These conditions or requirements should be kept up to date and would be subject to change to minimise the harm

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<sup>565</sup> *Macris v Financial Conduct Authority* [2017] UKSC 19, [2017] 1 W.L.R (SC).

<sup>566</sup> The FCA Enforcement Guide (4.30-33).

<sup>567</sup> IOSCO 4 IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 18 March 2020.

caused by a violation. Furthermore, a list of all the violations and their definitions is required to help CMA staff to ensure compliance with the CML.<sup>568</sup>

Finally, the CMA has the power to impose increased supervision on a suspected violator. This is a new power granted to the CMA, and it currently has no specification or limitation.<sup>569</sup> Although it is potentially useful, it is broadly stated and in practice may cause an overlap in supervision. For example, how can the CMA impose intensive supervision over a firm or bank that is licensed and supervised by another supervision authority, like an insurance company under MOCI supervision or a bank under CBK supervision? It causes an overlap in supervision. Another important consideration in the CMA's decision to impose intensive supervision would be any overlap with the Disciplinary Board's imposition of administrative sanctions. The CML sets out procedures to ensure that firms are treated fairly, but without published investigation reports there is a lack of transparency and hence inconsistency in handling misconduct.

In summary, while it is acceptable to give the CMA discretionary power to decide on how violations should be handled once an investigation is complete, this discretion must be used in accordance with a clear legal framework. It is submitted that the final stage of the investigation process needs reconsideration and further amendment to help ensure that all violators are treated equally.<sup>570</sup> The regulator's capacities to investigate in financial matters help to emphasise trust in the financial sector, but trust depends on the ability to punish non-compliant firms. It is suggested that the CMA uses similar practices to the FCA to improve the current investigation scope. It is important to change the CMA strategy so as to use resources intensively. The CMA must organise its priorities to enable it to extend its scope of work, while the investigative tools and powers must ensure that firms get fair treatment.

### 5.1 Settlement of cases

When a violation of the law has been proven, there is an option to settle the matter before it reaches the final enforcement decision.<sup>571</sup> In the event of a breach of the law, firms usually prefer to settle the matter out of court to protect their reputation and minimise damage. When

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<sup>568</sup> Amani K. Bouresli, above, (n 63) 78.

<sup>569</sup> Executive Bylaw, Module Three, Chapter Four, Article 4-13: 'The Authority may warn a Violator to cease committing the Violation and require him to undertake not to repeat it in the future *as well as subjecting him to additional supervision.*' (Emphasis added.)

<sup>570</sup> Angela Hayes and Carlos Conceicao, above (n 464) 293.

<sup>571</sup> CML, Article 131.

the reputation of a firm is damaged it loses investors' and shareholders' confidence, so using any opportunity to protect the firm from this is viewed as best practice.<sup>572</sup> The regulator must adopt a clear legal framework to ensure that the public interest is served. It is essential to ensure that the procedures and requirements for settlement are fair, effective and efficient and that they keep the ultimate objectives in mind, which are to protect the market and investors and act in the public interest.

In Kuwait the CMA has the power to settle ('reconcile') a matter with any firm at any stage of the criminal case before the final judgment is rendered, but this power is not absolute.<sup>573</sup> Matters that are subject to settlement are restricted to certain areas: only crimes that are stipulated in CML Articles 122, 124, 126 and 127, including insider dealing and market manipulation,<sup>574</sup> can be the subject of settlement under Article 131. In a case of insider dealing in stock markets, settlement is an option for the secondary insider only, not the primary insider. Another key point is that the settlement agreement involves a monetary payment, which should not be less than the minimum amount of the prescribed fine and not more than the maximum amount of that fine.<sup>575</sup> In addition to paying the settlement amount, any benefit achieved or losses avoided must be refunded, and the accused must not be a recidivist.<sup>576</sup> In other words, the settlement must ensure that the firm will be properly punished for its breach of the law. Furthermore, the CMA sets out the timetable for the firm to fulfil the reconciliation conditions.<sup>577</sup> The settlement decision – without mentioning any detail – is published on the CMA website.<sup>578</sup> These conditions and requirements are important to ensure fairness and protect the markets. The outcome of the settlement agreement will end any criminal cases pending in the court between the two parties (the CMA and the firm), but this does not prevent any third party from filing a civil case seeking compensation or the enforcement of any other rights.<sup>579</sup> Note that just as there is differentiation between civil and criminal rights in any matter, the settlement agreement with the CMA only suspends the criminal procedures; this

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<sup>572</sup> Mohamad Mostafa, *Economic Crisis* (2<sup>nd</sup> Edition, no publisher, 1979), part one, 215.

<sup>573</sup> Note that the English translation of the CML uses the term 'reconciliation' in article 131 rather than 'settlement' but the same meaning is intended and therefore the terms are used interchangeably in this discussion.

<sup>574</sup> CML, Article 122

<sup>575</sup> CML, Article 131.

<sup>576</sup> *ibid.*

<sup>577</sup> *ibid.*

<sup>578</sup> Executive Bylaws, Module Three, Chapter Seven, Article 7-3.

<sup>579</sup> Jalal S Othman, above, (n 544) 979-980.

gives other parties the chance to protect their rights and obtain compensation for a wrongful act committed against them by a firm.<sup>580</sup>

In some cases the existence of multiple supervisory authorities creates complications in achieving a settlement. For instance, if the investigated firm is a bank it is regulated by both the CBK and the CMA. In this scenario, regulatory wrongdoing overlaps with potential criminal misconduct. In other cases the prosecutors may claim that possible prosecution could be harmed if regulatory settlements are reached. Another complicating factor in the settlement of cases is the involvement of individuals who are facing penalties for misconduct related to the action that the regulator is taking against the firm. The firm certainly wants to settle quickly to protect its reputation, but the individuals want to clear their names because the allegations may have career-ending ramifications.<sup>581</sup>

The current legal framework for the settlement of cases under the CML is unclear and there are areas that need further development to improve the system. First, further conditions and procedures are required to cover all settlement agreements. For example, if a firm does not fulfil the conditions in the agreement, or if it does not abide by the required timetable, the CML has no provisions to cover what should happen next.<sup>582</sup> An unclear legal framework does not comply with IOSCO standards, which emphasise the importance of having a clear and consistent regulatory process.<sup>583</sup>

Secondly, it is submitted that settlement agreements with non-compliant parties do not comply with principles of fairness and equality, because well-established large firms will not suffer as much as small firms.<sup>584</sup> The financial implications could be greater for small firms which have not made provision for non-compliance, while large firms may have a budget specifically for satisfying regulators in the event of non-compliance. Although the regulator can set the settlement amount, at least one author has argued that there is a lack of fairness between big and small firms in respect to the settlement process because small firms may find it more

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<sup>580</sup> Ibid. 980.

<sup>581</sup> Angela Hayes and Carlos Conceicao, above (n 464) 4.

<sup>582</sup> Hussain Bouareki, 'For more determinate settlement procedures in the CMA' *Al-Qabas newspaper* (Kuwait, 22 March 2016) (in Arabic) <<http://alqabas.com/6442/>> accessed 13 March 2020.

<sup>583</sup> Principle 4 of IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 18 March 2020.

<sup>584</sup> Jamal AlOthman, above, (n 544) 501.

difficult to pay the fines as compared with well-established large firms.<sup>585</sup> It is difficult to confirm the soundness of this argument because the CMA only posts a basic notice of settlement decisions on its website, and does not publicly release the financial details of individual settlements. Fairness and transparency are principles emphasised by the IOSCO standards.<sup>586</sup> It is unfair that the CMA does not provide guidelines about settlement agreements, as this would give all firms the same opportunity to agree a settlement with the CMA.

Thirdly, the settlement process is arguably inconsistent with constitutional principles because the agreements are considered as verdicts, the rendering of which is supposed to be exclusively within the jurisdiction of the courts. Article 50 of the Kuwait Constitution confirms that there is a separation of powers between the three branches (legislative, executive and judicial), and none of them is allowed to waive part or all of its jurisdiction.<sup>587</sup> Only the judicial branch has the power to review cases and issue a verdict.<sup>588</sup>

Regardless of these arguments, it is important to have settlement agreements in stock markets because the markets are dealing with commercial and financial matters that are inherently related to economic stability. Thus it is useful to give the regulator the flexibility and discretion to settle some matters. If, for instance, a large firm is bankrupted because of substantial fines or compensation payments it will affect the whole market, thus settlements are a tool which can be used to protect both consumers' rights and the markets. It is important to note that the cost of an enforcement programme is reduced when the CMA settles a case, so the regulator should be equipped with the ability to dispose of cases efficiently.<sup>589</sup> In addition, it should be acknowledged that the natural act which is the basis of the criminal actions stipulated in the CML is different from crimes specified in other laws, because the act itself is not considered to be criminal (e.g. buying and selling shares). If this legal act involves other circumstances (e.g. insider information), it then becomes a breach of the law. Hence it is essential to provide some flexibility to the regulator in applying the law so that it has the discretion to reach appropriate settlements with individuals and firms who are unaware of the legal consequences

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<sup>585</sup> Mohamad Mostafa, above (n 572) 220.

<sup>586</sup> Principle 3 of IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 11 March 2020

<sup>587</sup> Kuwait Constitution Law, Article 50.

<sup>588</sup> Tamer Salah, 'Criminal Protection for Financial Markets – Comparative Study' (Alexandria, Dar AlJamea AlJaded, 2011) 486.

<sup>589</sup> Ana Carjaval and Jennifer Elliott, above (n 424) 21.

of their actions. In summary, there is a need to update the settlement provisions to give a clear legal framework for settlements under the CML. That updating should include adding new requirements and conditions to protect the market from abuse of this power.

The researcher asked the interviewees for their opinions of ‘the settlement agreement procedures in general and whether they provide a clear and fair framework to settle disputes as necessary in the financial sector’. The experts confirmed that the settlement arrangements need further development to provide clear and equal treatment for regulated firms.

Participant No. 1:

The idea of having settlement agreement as an option in the financial sector is a good development because it saves time and effort to end litigation. This tool needs a lot of development in regards to the conditions, and techniques required to guarantee transparency and equality in the market.

Participant No. 2:

It is a developed practice to allow a listed company that committed a crime for the first time to settle without ruining their reputation. It serves the objective of the law of deterring and punishing the company by imposing a penalty, without damaging its reputation. In fact, in the beginning the CMA policy was not to publish any settlement agreement, to avoid any criticism about their role to gain profit from fining the listed companies, but now I believe that the CMA should publish the settlement agreement without revealing confidential information to ensure transparency in dealing with listed companies.

Participant No. 3:

In terms of the settlement, there is no guidance or instructions regarding the settlement procedures. The current situation is vague. The CMA must issue instructions to provide an explanation about what type of crime can be settled and procedures about the settlement. Furthermore, the settlement agreements that have been reached must be published in their annual review with some details about the type of crime and the CMA policy in this regard. The CMA took huge amounts (double the specified fine) from violator companies in some cases. This is a custom that the CMA used to agree to settle any settlement but it is not written in any guidelines or instructions. It is necessary to be transparent about the settlement procedures.

Participant No. 4:

There are no publications in regards to the final settlement procedures. What is the role of the CMA to provide the market with a mechanism and policies towards settlement cases? Unclear and unpublished procedures kill the people’s trust in the



market. Does the CMA just settle with big companies only? What are the standards to reach a settlement?

Participant No. 5:

The settlement procedure is one way to punish the non-compliant firm without taking the long path. It needs some consideration to be used wisely but of course it is necessity in the financial sector.

Participant No. 6:

I believe they are unfair procedures to settle with a few non-compliant firms without providing clarification about this settlement. The procedures must protect the markets, not a few powerful companies.

Participant No. 7 said:

All the developed countries have this option to settle a dispute in a commercial matter, but it needs further amendment to ensure equality to serve the public interest.

In the UK the legal framework for a settlement agreement with the FCA is clear and adequate. The FCA's Enforcement Information Guide provides guidance and clarification about settlement cases.<sup>590</sup> The FCA Handbook also sets clear provisions for a settlement arrangement and its procedures.<sup>591</sup> The purpose of a settlement agreement, as stated in the FCA Handbook, is to save the FCA and industry resources, to compensate consumers at an early stage and to send a clear deterrence message to industry.<sup>592</sup> Unlike the CMA, the FCA settlement arrangement might not include a monetary payment and there is no determination in terms of the type of misconduct in the markets.<sup>593</sup> It provides great discretion to the FCA to settle any cases to secure its statutory objectives. There is a discount for early settlement of cases to encourage non-compliant firms and individuals to come forward. In fact, the majority of settled cases settle at Stage 1 of the executive procedures.<sup>594</sup> Complicating factors – multi-agency supervision and individuals' rights to clear their names – exist in both the UK and Kuwaiti systems. The UK legislation has struck a good balance between protecting individuals' rights and achieving effective regulatory enforcement. Under FSMA s. 393, if the FCA wishes to

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<sup>590</sup> The FCA, 'Enforcement Information Guide' available <<  
<https://www.fca.org.uk/publication/corporate/enforcement-information-guide.pdf>  
>> accessed 18 March 2020.

<sup>591</sup> The FCA Handbook, The Enforcement Guide, EG5.1

<sup>592</sup> *ibid.*, EG5.1.1

<sup>593</sup> *ibid.*, EG5.1.3

<sup>594</sup> Angela Hayes and Carlos Conceicao, above (n 464) 4.

make public an enforcement ‘warning notice’ against a firm, it needs either to refrain from identifying any individuals or to afford such individuals their ‘third-party rights’. Until 2010 the FSA could only publish details of its case against a firm when a ‘final notice’ was issued at the conclusion of the case. However, the Financial Services Act 2012 gave the FCA the power to publish details about an enforcement action much earlier, and ‘notably before a firm or an individual under investigation has had an opportunity to formally challenge the FCA’s case against them’.<sup>595</sup> In Kuwait the CMA could use this solution and refrain from identifying any individual in a notice to prevent delays in settlement procedures. In any case, it is important to set out a strong framework for settlement agreements because it relates directly to the protection of consumers and markets.

## **6. Enforcement powers**

This section investigates the CMA’s powers to punish and deter firms which commit a violation of the CML and its Executive Bylaws. The CMA uses discretionary administrative procedures to punish non-compliance. This administrative enforcement is not used for listed companies or individuals involved in insider trading in stock markets, because this is considered a criminal offence and must be investigated by a prosecutor and judged in court. It is important to investigate how the CMA deals with non-compliant firms, including listed companies which fail to comply with the obligation to disclose material information that might lead to insider trading. An effective policy against these companies is essential if the CMA is to succeed in enhancing investor trust in its ability to protect the stock markets from insider trading.

The administrative enforcement decision aims to *punish* firms and individuals for breaches of the law, and to *deter* future breaches. Essential to an understanding of the decision-making process is the recognition that it is administrative in nature rather than judicial. It enables the financial regulator to take enforcement decisions, which have a binding effect, without the need for sanctions from a court. The varieties of administrative sanctions provide a very broad spectrum of methods to ensure compliance. With an effective enforcement system ensuring that listed companies comply with the disclosure regime, the CMA can prevent insider trading in stock markets.

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<sup>595</sup> Allen & Overy ‘The FCA confirms its approach to publishing information about enforcement warning notices’ 23 October 2013 <<http://www.allenoverly.com/publications/en-gb/Pages/The-FCA-confirms-its-approach-to-publishing-information-about-enforcement-warning-notice.aspx>> accessed 18 March 2020.

After the issue of the CML in 2010, enforcement actions increased year by year. In the financial year 2015/2016 the total number of violations was 161, while in 2016/2017 this number increased dramatically to 309.<sup>596</sup> Some penalties were challenged through judicial review.<sup>597</sup> According to the CMA annual report of 2016/2017, there were 192 registered cases in the courts awaiting judicial review and 73 had reached the final verdict; only six cases went against the CMA.<sup>598</sup> Thus it can be seen that the CMA has the ability to use its power. The enforcement role is vitally important because it ensures the regulator has the tools and power to deter non-compliant firms and individuals, which in turn protects both markets and consumers.

In Kuwait, the Disciplinary Board has jurisdiction to review violations that any firms or individuals commit against the CML, its Executive Bylaws or ‘any law, or decision or instructions’ issued by the CMA.<sup>599</sup> However, the Disciplinary Board cannot investigate violations of any other laws, such as the customs laws. This means that the Disciplinary Board’s scope of work is related solely to the CML, which should help ensure there is no duplication between the supervisory authorities.

In the UK system, both regulatory authorities – the FCA and the PRA – have powers to impose disciplinary sanctions within their jurisdiction. Under the regulatory architecture, the FCA is responsible for most enforcement actions. The statutory provisions relating to the procedures for taking enforcement action are contained in FSMA Part XXVI, as amended by the Financial Services Act 2010 and the Financial Services Act 2012. Furthermore, the FCA sets out detailed procedures in the FCA Handbook DEPP module, released in June 2013.<sup>600</sup> Finally, the Enforcement Guide issued on 1 April 2013 describes the FCA’s approach to exercising its main enforcement powers<sup>601</sup> and gives an overview of the matters that will be investigated or resolved informally.

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<sup>596</sup> The CMA Financial Report 2016/2017,

<sup>597</sup> Ali AlKhaldi ‘Capital Markets Prosecutor’ *AlQabas* (Kuwait, 17 September 2017) available at <<https://alqabas.com/435715/>> accessed 18 February 2020.

<sup>598</sup> The CMA Financial Report 2016/2017 available << <https://www.cma.gov.kw/ar/web/cma/annual-reports>>> accessed 19 February 2020.

<sup>599</sup> Executive Bylaws, Module Three, Chapter Four, Article 5-2.

<sup>600</sup> FCA, Handbook DEPP module, available at <<https://www.handbook.fca.org.uk/handbook>> accessed 18 March 2020.

<sup>601</sup> FCA Enforcement Guide 1.1 Overview, 1 March 2016 <<https://www.handbook.fca.org.uk/handbook/EG/1/?view=chapter>> accessed 18 March 2020.

It is noteworthy that the FCA has adopted a strategy of ‘credible deterrence’, which has had four effects. First, the strategy has raised the level of penalties imposed on individuals and firms. The DEPP states that ‘If the FCA considers the [penalty] is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches then the FCA may increase the penalty.’<sup>602</sup> Secondly, credible deterrence has been used to hold senior individuals personally to account; examples of this strategy being employed by the FCA include the fine of nearly £120,000 imposed on Yohichi Kumagai, the former executive chairman of Mitsui Sumitomo Insurance Company, in May 2012, and the fine imposed on Peter Cummings, a former executive director of HBOS plc and chief executive of its Corporate Division, in September 2012.<sup>603</sup> These fines are the embodiment of the strategy’s goal, which is to hold individuals to account with strong enforcement action. The third effect is that credible deterrence has increased the regulator’s criminal prosecution power. Finally, the strategy has helped to develop the enforcement tools and power in the UK’s financial markets. Collectively, these improvements could, in the long term, lead to better overall protection of the markets from future financial crises by enabling the regulator to enforce adequate and appropriate sanctions effectively.

### 6.1 Precautionary procedures

When the regulator and regulated do not reach to a settlement agreement, a violator will be subject to fines and penalties. To ensure that violators do not destroy any evidence, it is vital for a financial regulator to have the power to take immediate action and/or precautionary measures to prevent any damage: quick implementation of such measures enables the regulator to minimise the damage.<sup>604</sup> For example, the regulator has the power to freeze assets, impose injunctions, suspend trading or suspend the activities of regulated firms. The aim is to prevent perpetrators from hiding the evidence by distributing assets to family and friends.

In Kuwait the CMA must refer the matter to the Capital Market Prosecutor for further investigation and deterrence if a firm allegedly committed a crime,<sup>605</sup> and can request the prosecutor to take precautionary procedures against the firm. The precautionary procedures could be to suspend a person from work temporarily, ban a person from travel or prevent a

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<sup>602</sup> DEPP 6.5A.4 ‘Step 4 – adjustment for deterrence’, 1 April 2013.

<sup>603</sup> Angela Hayes and Carlos Conceicao, above (n 464) 3-4.

<sup>604</sup> Ana Carjaval and Jennifer Elliott, above (n 424) 18.

<sup>605</sup> Executive Bylaws, Module 3, Chapter 6, Article 6-3

person from managing his/her money.<sup>606</sup> These measures are available in addition to the normal precautionary procedures under the Civil Procedures Law. The CML takes into consideration the nature of the commercial matters that are related to the market, and imposes a timeline for the prosecutor to respond to the CMA's request to start precautionary procedures: the prosecutor must make a decision within 24 hours from the time of submission of the request.<sup>607</sup> In the event that the request is rejected, the cause of refusal must be stated. The obligation to state the cause of rejection can be challenged by the CMA, to ensure that decisions are made on a sound legal basis. The Capital Market Prosecutor is the only authority with the power to impose precautionary procedures, and the CMA cannot take any precautionary steps without the prosecutor's order. The procedures relate to a person's rights of freedom and managing his/her money, so it is necessary to protect these rights carefully from any abuse of power and ensure that orders from the prosecutor are kept to a minimum.

It is worth mentioning that giving the CMA the power to use the precautionary procedures is important to comply with IOSCO standards. All these elements and factors are addressed in IOSCO Principles 10–12 regarding the necessary legal framework for enforcement law. Having adequate precautionary procedures can protect the markets from non-compliant firms and ensure they are punished.

## 6.2 Enforcement decisions

If it is satisfied that a violation has been committed, the Disciplinary Board may issue any of the following penalties.<sup>608</sup>

1. Cautioning the violator to discontinue committing the violation.
2. Issuing a warning.
3. Requiring the violator to re-pass pre-qualification tests.
4. Suspending his/her activities for a period not exceeding one year.
5. Suspension from practicing work or profession in final.
6. Suspending the license for a period not exceeding six months.
7. Revocation of the license.
8. Imposing restrictions on the activity or activities of the violator; such restrictions shall be specified by the CML Bylaws.
9. Canceling the voting or proxy or power obtained by the violation of the provisions of the CML.
10. Suspending or canceling any acquisition offer or purchase transactions outside the scope of the acquisition offer if they are in violation of the provisions of Chapter 7 of CML or the Bylaws.
11. Prohibition of exercising voting rights for a period not more than three years by any Person who refrained from submitting any statement, or submitted an incomplete statement, or one contrary to the truth or in violation with the CML

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<sup>606</sup> Executive Bylaws, Module Three, Chapter Seven, Articles 6-2 and 6-3.

<sup>607</sup> *ibid.* Article 6-4.

<sup>608</sup> CML, Article 146.

or the Bylaws. 12. Suspending the validity of an applicable prospectus according to the provisions of CML. 13. Cessation of trading of a Security temporarily or suspension or cancellation of the decision to list a Security before the effective date thereof. 14. Dismissal of a member of a Board of Directors or of a manager of one of the licensed companies or listed companies or Investment Controller or Custodian of a Collective Investment Scheme who failed to perform his/her duties as provided in CML or the Bylaws. 15. Imposing financial penalties that are defined according to the severity of the violation not exceeding fifty thousand Kuwait Dinars.

In all cases, the Disciplinary Board may cancel all transactions related to the violation and the entailed effects, or require the violator to pay amounts equal to the benefit he/she acquired or the value of the loss he/she has avoided as a result of the violation. The amount may be multiplied if the Person repeats committing the violations.

The range of penalties is broad, which gives the Disciplinary Board flexibility. Enforcement includes the possibility of imposing financial penalties, as per Article 146(15). It is suggested that the power to impose fines is particularly useful because it exacts an immediate punishment on the violator while avoiding a potentially lengthy judicial process involving matters that may be difficult to prove in court.

#### 6.2.1 Interpretation of enforcement decisions

These penalties may be subject to interpretation by the Disciplinary Board, since there are no clear controlling guidelines to follow and no specified gradation in the application of penalties under the CML. There is no distinction between companies and individuals who commit violations. The same enforcement decision might be applied to a listed company with huge capital and to an individual; this is unfair punishment, as the individual will be damaged more than the firm. In the interviews, Participant No. 6 stated that the same financial penalties should not be imposed on firms and individuals (see below). It would be useful to determine, in a special section of the law, exactly what constitutes a breach in order to establish civil/administrative liability.<sup>609</sup> The IOSCO standards confirm the importance of having a clear and consistent legal framework.

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<sup>609</sup> Fatima AlShuraian, above (n 4), 102. Al Shuraian argues for the importance of ‘issuing a special section that describes market manipulation and prohibits it, directly and clearly, so that the nature of market manipulation is clarified...’

In the UK there are guidelines in the FCA Handbook describing in detail all the requirements and conditions for applying an enforcement decision.<sup>610</sup> The enforcement policy is designed to ensure that ‘the FCA is upholding regulatory standards and helps to maintain market confidence and deter financial crime’.<sup>611</sup> There is also a Decision Procedures and Penalties Manual which described the FCA’s decision-making procedure for issuing enforcement decision.<sup>612</sup> All those provisions provide a clear framework for the FCA to take an appropriate decision in punishing non-compliant firms and individuals.

As explained earlier, the CMA follows a tit-for-tat approach in imposing enforcement decisions. The compliance approach is part of the new CMA policy to enforce the law, but there is no categorisation of businesses<sup>613</sup> to enable fair application of this approach, and no consultation or dialogue with listed companies to ensure compliance. This is unlike the FCA, which has principles and policies to impose enforcement decisions on non-compliant firms. For example, the ‘come clean’ policy encourages non-compliant firms to step forward and disclose their errant activities.<sup>614</sup> Kuwait has no such policy, and also lacks compliance tools and mechanics, and incentives or rewards to encourage firms to admit their wrongdoing.

Thus the CMA should provide documentation containing definitions of all violations and breaches, plus guidance, examples and details of business categorisation and mechanisms to apply a compliance approach correctly.

Since there is no published guidance about the interpretation of enforcement decisions, the researcher asked the interviewees for their views on the CMA’s strategy regarding enforcement decisions in the financial sector: does this policy provide sufficient deterrence and is there anything to improve? The responses revealed a lack of knowledge about how the CMA interprets enforcement decisions and what the basis is for these decisions. Participants Nos 2 and 5 gave clarification about CMA policy, while the other six interviewees were not aware of CMA policy.

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<sup>610</sup> The FCA Handbook, The Enforcement Guide, EG7.1.1

<sup>611</sup> *ibid.*

<sup>612</sup> The FCA Handbook, DEPP Decision Procedures and Penalties Manual, Section 6.5A the five steps for penalties imposed on firms. <<https://www.handbook.fca.org.uk/handbook/DEPP/6/5A.html>> accessed on 30 January 2020.

<sup>613</sup> John T Scholz, ‘Voluntary Compliance and Regulatory Enforcement’ above, (n 433) 385. See Dalvinder Singh, above (n 21)117.

<sup>614</sup> *Ibid.* 116.

Participant No. 2 stated:

When the CML was first applied back in 2010, the CMA was very strict in terms of capturing the violations. For example, the CMA used to impose the maximum penalty on the non-compliant firms to deter others. Now, I believe that the CMA has changed their policy to adopt a more flexible 'compliance approach'. The aim is to correct the violation more than punish the listed company, but this policy must be improved to develop the markets. It is useful to have a compliance officer in the listed company to ensure the application of the CMA law and its bylaws. This compliance officer must be qualified to do so by having sufficient knowledge and education. Unfortunately, until now there is no academic institution that teaches CML law.

Participant No. 5:

The CMA adopts a strict policy to ensure compliance. The CMA has a process to investigate the information to understand its impact on the markets, especially on prudent investors. The disciplinary board has discretionary authority to decide whether this information is material or inside information. In fact, this investigation process in the CMA starts at the Disclosure Department to study the case and decide whether the information may be material information that must be disclosed or not. It sends the matter to the Legal Department to investigate, which reports back to the CMA Board to consider whether to refer the case to the Disciplinary Board or not. The Disciplinary Board issues a penalty if necessary. If the company has any objection about the Disciplinary Board's decision, it should file a complaint to the Complaint Committee in the CMA to investigate the case. Judges do not have the expertise to investigate very technical matters about stock markets. On the other hand, the CMA uses all these channels to ensure that a crime has been committed and the insider must be punished.

Participant No. 1 stated:

The CML has not set a certain policy to enforce the law to give the CMA the freedom to adopt the best appropriate policy. There is no published policy in this regard.

Participants Nos 3 and 4 believed that no policy has been published or adopted regarding enforcement decisions, while Participants Nos 6 and 7 felt that there is no guidance or published policy about the CMA strategy to enforce the law.



### 6.2.2 Financial penalties

Financial penalties are a great tool to punish and detect non-compliant firms,<sup>615</sup> but must be used only in extreme forms of misconduct. The regulator assesses various factors and elements to determine such misconduct and reach an appropriate decision. For example, the FCA reviews the seriousness of the misconduct and its impact on regulatory objectives.<sup>616</sup> There is no such procedure to determine the seriousness of misconduct in the CMA, and it does not follow any policy in terms of applying financial penalties. The lack of determinants to decide an appropriate financial penalty affects the effectiveness of the enforcement policy.

Furthermore, the maximum permissible financial penalty is insufficient. There is currently a limitation in CML Article 146(15) which provides that any financial penalties should not exceed 50,000 Kuwaiti dinars.<sup>617</sup> It should be noted that violations in stock markets involve figures that often far exceed this amount, and violations in commercial and financial markets can result in benefits that are measured in millions of dinars. For example, the Disciplinary Board imposed financial penalties against Mushrif for Trading and Contracting Company of 2,000 Kuwaiti dinars for violating the rules on disclosing material information (specifically, not reporting two lawsuits filed against the Ministry of Public Works for withdrawing two projects), followed by 50,000 Kuwaiti dinars for failing to keep the books and records accurately according to international accounting standards and transferring costs between projects.<sup>618</sup> The Mushrif company stopped trading in the stock market, which caused huge losses to the public and the market.<sup>619</sup>

Another incident indicates that the current financial penalties under the CML do not form an effective deterrent. On 4 January 2018 the CMA imposed a financial penalty against an investor for not submitting a mergers and acquisition proposal as the law required. The penalty was 5,000 Kuwaiti dinars, renewable monthly starting from 30 March 2018 if the investor did not correct the violation. Imposing a financial penalty plus a monthly renewal is not mentioned in

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<sup>615</sup> Dalvinder Singh, above, (n 21) 134.

<sup>616</sup> Ibid. 134

<sup>617</sup> This is the equivalent of approximately £124,000.

<sup>618</sup> Disciplinary Board Resolution No. 65/2017 issued on 29 November 2017 Available at <<https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/488317>> accessed 30 January 2020.

<sup>619</sup> Kuwait Stock Markets "Boursa" Website << <https://www.boursakuwait.com.kw/news-details/35245/0>>> accessed 18 March 2020.

CML Article 146(15), which proves that the current financial penalty in the law is insufficient to punish and deter the markets. The investor filed a case against the CMA based on the creation of a financial penalty that is not stated in CML Article 146. On 28 May 2018 the court of the first instance issued its verdict, stating clearly that the CMA does not have the power to impose a penalty not included in the CML, because the Kuwaiti system recognises only the letter of the law.<sup>620</sup> Regardless of the court verdict, the case confirms that it is necessary to amend financial penalties to achieve deterrence and ensure compliance with the law.

Thus it is important to reconsider the maximum allowable financial penalties. All penalties are important to ensure the enforcement of the law, the proper punishment of the offender and effective deterrence of future non-compliance.<sup>621</sup> The IOSCO standards confirm that the regulator must have sufficient power to enforce the law, and the limitation of financial penalties does not serve this objective. The current penalties as determined by CML Article 146 are very lenient and, it is submitted, do not achieve deterrence.

This stands in contrast with the UK approach: while the FCA can impose substantial fines on market manipulators, in Kuwait the CMA can only impose limited financial penalties. The financial penalties that the FCA can impose on a market manipulator range from zero up to 20 per cent of the firm's revenue from the relevant products or business areas.<sup>622</sup> The FCA guidance states that 'The amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breach may cause, and in such cases the FCA will determine a figure which will be based on a percentage of the firm's revenue from the relevant products or business areas.'<sup>623</sup> Finally, as mentioned above, the FCA uses a compliance approach, so it could issue a public censure instead of levying financial penalties if this fits the criteria.

The interviews confirmed that limitation of financial penalties in Kuwait does not serve the regulator's objectives to punish and deter non-compliant companies. Only one of the

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<sup>620</sup> Case No. 18/2018 Capital Market Court, Administration Circle No.5.

<sup>621</sup> Principle 11 of IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 11 March 2020

<sup>622</sup> The FCA Handbook, DEPP Decision Procedures and Penalties Manual, Section 6.5A the five steps for penalties imposed on firms. <<https://www.handbook.fca.org.uk/handbook/DEPP/6/5A.html>> accessed on 30 January 2020.

<sup>623</sup> The FCA Handbook, DEPP Decision Procedures and Penalties Manual, Section 6.5A the five steps for penalties imposed on firms. <<https://www.handbook.fca.org.uk/handbook/DEPP/6/5A.html>> accessed on 30 January 2020.

participants disagreed with this argument: Participant No. 2 was convinced that this limited financial penalty can deter and punish the non-compliant.

Participant No. 2:

The 50,000 Kuwaiti dinar as a maximum fine is sufficient if we take into consideration that the violator has to return the benefits or the losses that they avoided while exercising illegal activities such as insider dealing.

The rest of the interviewees disagreed with this view.

Participant No. 1:

Reality shows that the limitation of the financial penalty does not provide sufficient deterrence, especially with recent events with a company that did not provide correct financial statement and the penalty was unfair for the shareholder.

Participant No. 3:

Limiting a maximum financial penalty is mentioned in Article 146 in CMA law, which is the most insufficient provision of the law because it does not provide suitable and deterrent punishment for financial crimes. In fact, the CMA imposed a fine against a listed company to pay 5,000 on a monthly basis, but the court annulled this fine as it is unconstitutional. A new punishment was added by the authority that wasn't approved by law.

Participant No. 4:

The limitation of the financial penalty in Article 146 is a disaster. It deals with companies that have capital or net profit in millions of Kuwaiti dinars and punishes them with a maximum fine of 50,000 Kuwaiti dinars. This is like a 'reward' for their non-compliance. The CMA's deterrent approach is incompliant with its purpose, when putting such minimal punishment for companies that have a value of over a million.

Participant No. 5:

The limited financial penalty that Article 146 provided is insufficient of course. In practice, the CMA punished companies that violated CML law. After a period of time the same company committed the same violation (not insider dealing, other violation) because the income of the violation is greater than the financial penalty which is 50,000 Kuwaiti dinars, therefore it was not enough to punish a company with that amount if it had a huge capital and business.

Participant No. 6:

The punishment provision does not provide a deterrent approach at all. First, there is no fairness if a company and a trader face the same punishment if they committed

the same crime. The trader will be more harmed and punished than the company. For example, if an investor has 70,000 Kuwaiti dinars to invest in stock markets and the punishment reached 12,000, it is a huge loss for him. On the other hand, a big company has a capital reaching 1,000 million in value. The punishment should be fitting the company's financial status. Secondly, the financial penalty is limited and does not provide sufficient punishment. For example, some companies violate the law intentionally. If the trade in stock markets is very slow due to unstable circumstances like political circumstances, companies do not disclose their financial statement on purpose to allow the CMA to halt their shares in the stock markets. In that case, the CMA halt cannot be considered as punishment because the company broke the law to enforce the CMA to halt/stop their shares in those unstable and unusual circumstances. So how can this limited financial penalty deter this kind of practice?

Participant No. 7:

The recent cases showed how the limited financial penalty does not provide sufficient punishment or deterrence. Firms continue to commit the same violation without being deterred.

### 6.2.3 Conflict of interest

There is another key element of the enforcement regime that should be subject to amendment. Once a violator has paid a fine, the funds go into the CMA's budget and become part of its financial resources. Although this is probably well intentioned, to offset the cost of regulation and enforcement, it creates a conflict of interest because the CMA might be tempted to increase the size and number of fines.<sup>624</sup> This arrangement seems wrong in principle. In the UK the penalties go to the Treasury after deducting enforcement costs.<sup>625</sup> It is important for Kuwait to amend the law so that financial penalties are paid to the MOCI or the Ministry of Finance to avoid this conflict of interest.

Furthermore, the IOSCO Principles address conflict of interest in pursuit of market stability,<sup>626</sup> saying it is necessary to give regulated persons protection from abuse of regulatory power. The IOSCO standards confirm that to have effective enforcement law, financial regulation must be above conflicts of interest.

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<sup>624</sup> CML, Article 19.

<sup>625</sup> Financial Services Act 2012, Schedule 1ZA s 20.

<sup>626</sup> Principle 5 of IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 11 March 2020

#### 6.2.4 Publication

Another area of concern is the publication of penalties. It is CMA practice to publish all penalties on its website. This is arguably a violation of privacy and confidentiality rights, which must be afforded priority. The Kuwait Constitution provides that there must be no punishment without a law stating that the act is forbidden.<sup>627</sup> CML Article 146, which sets forth an exhaustive list of all the penalties that the Disciplinary Board can impose, does not include anything related to publication of imposed penalties.<sup>628</sup> Thus the legislature needs to pass a law that specifically permits the CMA to publish the penalties it imposes. The current situation is unacceptable and arguably unconstitutional, and there is a need for the CMA Board to consider this issue further. Publication not only affects the reputation of the penalised firms and individuals, but may also lead to the identification of third parties, which should be protected from any publication. The interviews confirmed the weakness of the CMA's practice of posting Disciplinary Board decisions with the non-compliant names and all related detail. Although it gives transparency in the markets, the law does not allow such posting of punishments on the CMA website. It is worth mentioning that this publication is an application of the IOSCO Principles to provide transparency and fairness to regulated firms.<sup>629</sup> It gives the regulated an idea of the thematic pattern that the CMA follows to enforce the law. Also, it gives guidance to regulated and non-regulated markets to be aware of the firms committing the most violations, which helps to protect the markets.

Participant No. 1:

The CMA is not willing to change their practice and publish all violations on their website to ensure the transparency of the market. It might be useful to reform the law to add publication of the violation.

Participant No. 2:

Publication of violations is part of the CMA policy, to impose a strict strategy to enforce the law. It is important to provide transparency to the markets. I believe, to better enforce decisions, it might be a good development to amend the law to refer to the publication as punishment.

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<sup>627</sup> Kuwait Constitution, Article 32.

<sup>628</sup> Hussain Bouareki, above (n 4**Error! Bookmark not defined.**) 354.

<sup>629</sup> Principle 4 of IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 11 March 2020.

Participant No. 3:

It is an extremely wrongful and illegal practice for the CMA to publish the disciplinary decisions on their website without a law to that effect. Publishing disciplinary decisions is a punishment that needs a provision in the law to allow it. The publication includes the violator's name and title, which is against the protection of privacy of the violator, and even the final court judgment should not go public as the CMA disciplinary decision, thus the practice of publishing must end as soon as possible.

Participant No. 4:

Although it is a good practice to publish the disciplinary decision, the practice does not protect the privacy of the violator. If I imagine myself as a violator, it will affect my work and reputation, therefore it must be according to the written law.

Participant No. 6:

The CMA published a disciplinary decision and it was someone I knew. I believe this publication destroyed his reputation. I believe that the CMA must amend the law.

Participant No. 7:

According to the constitutional and criminal laws, publication of the violator's names is a punishment, which must be stated in the law. Well this is your answer. The CMA has no right to publish the disciplinary decision without a written provision.

In the UK, FSMA s. 391(7) and the DEPP govern the manner of publication. Section 391(7) states that information will be published in a manner that is determined by the FCA, according to the circumstances of the situation. Unlike in Kuwait, authorisation to publish is specifically provided for by law. Thus final notices may be published in accordance with the law and at the discretion of the FCA. In some circumstances the FCA may decide not to publish the information, if it will be unfair to the person or to protect the markets.<sup>630</sup> The publication takes the form of a release on the FCA's website. It includes a summary of the case, comment from a senior member of the FCA's staff and a copy of the final notice. The concerned person can comment on the final notice with 24 hours of publication.<sup>631</sup> This opportunity to comment on

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<sup>630</sup> Financial Services Act 2012, s 397(4) (6).

<sup>631</sup> Angela Hayes and Carlos Conceicao, above (n 464) 259.

the final notice is important for the firms and individuals to emphasise the transparency in the markets. Moreover, the FCA adopted a new policy in 2010 regarding the enforcement of financial penalties, as a result of which the amount of fines increased. This is reflected in the FCA's Enforcement Guide (2016), section 6.2.16:

Publishing a notice is important to ensure the transparency of FCA decision-making; it informs the public and helps to maximize the deterrent effect of enforcement action.

Furthermore, the recent Supreme Court decision in *Macris v Financial Conduct Authority* gives an important basis for publishing public notices regarding the outcome of an investigation.<sup>632</sup> The court confirms that the publication of the notice serves the public interest in the proper performance of the FCA's functions, and emphasises the importance for the public interest of knowing the finding of a particular investigation.<sup>633</sup>

#### 6.2.5 Objection procedures

Any person who has received a penalty pursuant to CML Article 146 may appeal in writing against the Disciplinary Board's decision. However, it seems that this appeal process is not an effective review and second look at the enforcement decision. The appeal must be made to the CMA within 15 days of receiving written notification of the penalty. The CMA Board will refer such an appeal to the Disciplinary Board for further consideration so that it may issue its final decision. The same member of the Disciplinary Board will review the objection as took the initial decision, thus there are no effective procedures to examine and investigate the objection. In practice, there are two possible outcomes. The first scenario is that the Disciplinary Board could uphold the appeal and modify the enforcement decision. The second scenario is that the Disciplinary Board could decline the appeal, either explicitly or implicitly. If the board does not respond to the concerned person within 30 days from submitting the appeal, the person should consider this as an implicit refusal. It is recommended that another Disciplinary Board, with different members, should review an appeal to ensure fairness and impartiality. The current situation leads to a rejection of all appeals against the Disciplinary

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<sup>632</sup> *Macris v Financial Conduct Authority* [2017] UKSC 19; [2017] 1 W.L.R. 1095 (SC).

<sup>633</sup> *Macris v Financial Conduct Authority* [2017] UKSC 19, [2017] 1 W.L.R. (SC).

Board's decisions.<sup>634</sup> In the UK, the RDC is the final stage of FCA decision-making,<sup>635</sup> and there is no appeal process in the legal framework. The RDC is an administrative body to review violations and issue enforcement decisions without any role in the objection process. In practice, there is no point in having objection procedures if the same person will review the matter and issue (most probably) the same outcome, thus it might be useful if Kuwait waives this obligation to submit an appeal to the Disciplinary Board in the first instance and gives regulated persons the chance to file an appeal directly to the court to save time and effort.

It is noteworthy that the CMA addressed the objection procedures to comply with the IOSCO standards to have a consistent regulator process. It provides the regulated with the same chance to review the matter before them using judicial review. But although it might indicate the good intention of the regulator, it does not prove effective in the market.

## **7. Conclusion**

This chapter explores the CMA investigative and enforcement power to ensure compliance. A number of areas are identified wherein Kuwait can improve its regulatory enforcement.

In terms of overall approach, the analysis of Kuwait's enforcement law architecture shows that the CMA is focused only on deterrence without using a compliance approach. There are no tools and mechanisms to encourage a non-complaint firm to come clean or incentives for compliant firms. Although the CMA enforcement strategy has recently been developed to adopt risk-based and compliance approaches to inspection, no guidance has been published.<sup>636</sup> The key element in an effective compliance approach is dialogue and communication between the regulator and the regulated, but the current practices show no encouragement or any policy in this regard. This affects the application of a compliance approach.

The deterrence approach is resource-intensive and involves high costs and a time-consuming process to issue final enforcement decisions. A good enforcement strategy can reduce both enforcement and compliance costs by encouraging cooperation rather than confrontation between the regulator and regulated firms.<sup>637</sup> To be fair, the compliance approach has only

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<sup>634</sup> The CMA Financial Report 2016/2017.

<sup>635</sup> Financial Conduct Authority, *Enforcement Information Guide*, (2017).

<sup>636</sup> The CMA, 'Guidance on The CMA's Internal Inspection' (unpublished June 2019).

<sup>637</sup> John Scholz, Voluntary Compliance and Regulatory Enforcement' above (n 433) 385.



recently been adopted in Kuwait, so the CMA needs time to change the industry culture and implement the compliance tools and mechanisms.

Another key reason to support the compliance approach is that the deterrence approach cannot achieve complex purposes because it is inherently difficult to write clear, unambiguous laws that have the desired effect and cover all possible situations.<sup>638</sup> The compliance approach creates an appropriate legal framework that can take into consideration complex situations a firm may face and provide considerable discretion in resolving legal ambiguities to achieve the financial regulator's objectives. For example, in difficult situations a firm may breach the rules based on extraordinary circumstances, yet if the regulator applies only the deterrence approach the firm will be exposed to civil sanctions. By contrast, the compliance approach takes into consideration other circumstances that the firm may face on a daily basis. When relying solely on the deterrence approach, it is difficult to know when to make an exception and when to enforce the letter of the law because of the contingent nature of enforcement decisions.<sup>639</sup> Hence it is suggested that Kuwait should improve the new enforcement policy to embrace both deterrence and compliance approaches.

Furthermore, the above analysis shows that the CMA wields significant power. It can enter the premises of regulated firms without prior notice and it can seize and copy documents. CMA staff members, who are essentially granted a judicial power of investigation, can access the necessary records and books to obtain key information, which can help to prove that a crime has been committed. The wide investigative scope – which can involve third parties – emphasises the need for trust and confidence in the market. Great power has been entrusted to the CMA, but this creates a public expectation that the CMA is not there to merely work with the industry, but to take on a disciplinary role when circumstances mandate it. There is a limit to the CMA's ability to request information from third parties, and its power in this area is not as strong as the FCA's power in the UK. The FCA can involve not only the authorised person but also any person who is connected with an authorised person. Expanding the investigative scope so that it is on a par with that of the FCA could lead to even greater trust and confidence

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<sup>638</sup> Dalvinder Singh, above (n 21 **Error! Bookmark not defined.**) 115. See also John Scholz, 'Voluntary Compliance and Regulatory Enforcement' (n 433) 7, who makes a similar point at 387: 'There is a limit, however, beyond which rules and laws cannot match the complexity of the world they attempt to govern without becoming too complex for enforcement...even an elaborate set of rules cannot eliminate ambiguity caused by the bigness of the world...'

<sup>639</sup> John Scholz, 'Voluntary Compliance and Regulatory Enforcement' above (n 433), 387.

in the CMA and, ultimately, greater confidence in its ability to regulate the financial markets effectively.

In respect to the enforcement of decisions, the CMA needs to give further consideration to three areas: the maximum amount of financial penalties; the publication of violations on the CMA website; and the receipt of fines. For the first point, it is certainly an improvement to add financial penalties to CML Article 146, but the maximum penalty is set too low; the law needs to be amended and the current maximum amount needs to be substantially increased. For the second point, it is suggested that the CMA must amend the Executive Bylaws expressly to permit publication of CML violations on the CMA website. The current practice of publishing violations without any statutory permission needs to be resolved as soon as possible. The third point refers to the collection of financial penalties, and it is recommended that the money must not go directly to the CMA's budget to avoid a conflict of interest. It might be better for penalties to be paid to the MOCI or the Ministry of Finance.

In term of the settlement agreement system in the CMA, there is a need for further amendment to adopt conditions that will ensure all firms and individuals are treated equally. The law must set out a clearer legal framework for settlement matters and not leave it to the absolute discretion of the CMA. On the other hand, the CMA must prioritise confidentiality. The right to privacy and confidentiality must not be breached without reasonable evidence. The CMA should follow the FCA's policy regarding the protection of confidentiality and people's privacy. The UK laws related to banking confidentiality and legal privilege and the Data Protection Act 1998 contain iterations of the confidentiality principle, all of which should be carefully considered by the Kuwaiti legislature. Kuwait ought to amend the current framework to ensure better protection of the confidentiality rights of alleged and proven CML violators and third parties.

Finally, a transparent financial industry can ensure the stability of the economy and attract new investors. IOSCO Principle 10 states that the regulator should have comprehensive inspection, investigation and surveillance powers. A well-written legal framework must grant the financial regulator a clear mandate to enforce regulations. It is important for the regulated firms and individuals to be fully aware of the enforcement law to ensure its comprehensive implementation. A clear and transparent mandate creates public awareness of the tools and powers of the regulator, and fosters investor confidence and trust in the markets. If the mandate

to enforce the law and sanctions is not sufficiently clear, there will be a weakening of enforcement.<sup>640</sup> Thus it is essential to adopt a clear and transparent legal framework for enforcement.

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<sup>640</sup> IMF report 'The challenge of Enforcement in Securities Markets: Mission Impossible?' August 2009. 13.

## Chapter 6: Disclosure Regime to Tackle Insider Trading

### 1. Introduction

In the wake of the 2008 financial crisis, most policymakers focused on developing and improving regulation of the disclosure regime.<sup>641</sup> For disclosure in securities markets to be effective, information is key. Disclosure of material information affects the value of shares in stock markets positively or negatively, ensures equal access to information to prevent insider trading<sup>642</sup> and treats all listed companies equally in line with the fundamental principle of fairness.<sup>643</sup> Precisely for this reason, many jurisdictions reformed their disclosure regulations to ensure that the quality of disclosed information aids the fundamental goal of regulators: protecting market integrity and preventing insider trading.

The disclosure regime for listed companies in Kuwait is regulated by the CML and its Executive Bylaws.<sup>644</sup> It allows no exemptions from the obligation to disclose material information. This is a lesson stemming from the 2008 financial crisis: a regulator must be informed about market behaviour to pre-empt adverse events.<sup>645</sup> At the same time, disclosure obligations protect investors and increase their confidence in the stock market.<sup>646</sup> Disclosure helps to assess risk in stock markets and allows the regulator to set its priorities according to listed companies' risk profiles. The IOSCO Principles highlight the importance of having an effective disclosure regime to protect investors in the markets.<sup>647</sup>

A disclosure regime is a method to protect the stock market from insider trading.<sup>648</sup> It increases the efficiency of the investment process, given that investing is a complex task which requires

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<sup>641</sup> Emiliós Avgouleas, 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', 2-3 in Iain G Macneil (ed), *The Future of Financial Regulation* (1 edition, Oxford Hart Publishing 2010).

<sup>642</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' above, (n 12), 1584.

<sup>643</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 19 February 2020.

<sup>644</sup> Capital Markets Authority Kuwait, 'Executive Bylaw' (2015) <<https://www.cma.gov.kw/en/web/cma/-bylaw-documents>> accessed 10 February 2020, Module Ten.

<sup>645</sup> Emiliós Avgouleas, 'What Future for Disclosure as a Regulatory Technique? (n 641).3, see also Policy Statement on Financial Market Development (The President's Working Group on Financial Markets, March 2008)

<sup>646</sup> Luca Enriques and Sergio Gilotta, above, (n 423) 514.

<sup>647</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > accessed 30 January 2020.

<sup>648</sup> *ibid* 1565. See also Luca Enriques and Sergio Gilotta, above, (n 423) 515. See also Jamal AlOthman, above (n 544) 122.

specific analytical skills.<sup>649</sup> Ultimately, designing an effective disclosure regime is not a simple task for regulators – the law has to be robust both on paper and in practice. To achieve this aim, a disclosure regulation requires a listed company to disclose material information to market participants. An effective disclosure regime is based on two conditions: first, the regulation must ensure that investors receive sufficient information about the value of a company's business; and second, the disclosed information must be accurate. Both elements are essential for sustaining market-wide confidence.<sup>650</sup>

International organisations have raised this issue and offered recommendations to prevent insider trading and improve the disclosure regime. The Organisation for Economic Co-operation and Development (OECD), for example, has recommended that countries must adopt fair, timely and efficient mechanisms for disseminating information to investors.<sup>651</sup> IOSCO introduced principles to ensure that stock markets are fair, efficient and transparent.<sup>652</sup> A joint committee of the Basel Committee on Banking Supervision and the IOSCO Technical Committee determined that protecting the financial system requires ongoing revisions of disclosure and transparency rules and regulations to ensure that accurate information is disclosed and available to investors and market participants.<sup>653</sup>

In 2004 the IMF issued a report evaluating the Kuwaiti financial sector. It found that one of its weaknesses is a lack of regulation preventing insider trading.<sup>654</sup> In the period following the 2008 financial crisis, Kuwait adopted a new disclosure regime to protect the integrity of the stock market and the economy.<sup>655</sup> The first step in this process was the issue of the CML in 2010, which introduced new provisions regulating disclosure. The latest additions to the

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<sup>649</sup> *ibid.*

<sup>650</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets', above (n 12) 1566.

<sup>651</sup> OECD Principle of Corporate Governance (2004) available at <<https://www.oecd.org/corporate/ca/corporategovernanceprinciples/31557724.pdf>> 22 accessed 30 January 2020.

<sup>652</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 19 February 2020.

<sup>653</sup> Basel Committee on Banking Supervision and IOSCO, 'Recommendations for Public Disclosure of Trading and Derivatives Activities of Banks and Securities Firms' <<https://www.bis.org/publ/bcbs48.htm>> accessed 30 January 2020.

<sup>654</sup> International Monetary Fund, 'Kuwait: Financial Sector Assessment Program--Detailed Assessments of Observance of Standards and Codes--International Organization of Securities Commission (IOSCO)--Objectives and Principles of Securities Regulation' <<https://www.imf.org/external/pubs/ft/scr/2004/cr04352.pdf>> accessed 30 January 2020.

<sup>655</sup> CML.

regulations were the Executive Bylaws issued in 2015. This moved the CMA approach towards a market-driven, disclosure-based regime of supervision.<sup>656</sup>

The CMA is now keen to implement a full disclosure policy to achieve fairness and transparency and prevent abuse of inside information. It aims to provide investors with the information required to calculate risk effectively and make sound investment decisions.<sup>657</sup> The CMA has introduced provisions to enhance disclosure in the KSE (Boursa) by compelling listed companies to disclose material information, and in so doing enable the regulator to ensure transparency.<sup>658</sup> Unpublished material information then becomes inside information that an insider abuses to gain a profit or avoid losses.

Establishing an effective disclosure regime that protects investors is the responsibility of the regulator,<sup>659</sup> while the quality of information disclosed to the regulator affects investors' ability to understand market risks better.<sup>660</sup>

One reason for focusing on the Kuwait disclosure regime is pragmatic. A recent trend noted in the Kuwait stock market is the delisting of companies from the KSE. Before the 2008 financial crisis the KSE consisted of 224 listed companies.<sup>661</sup> After the 2015 amendments to the law were adopted, the number of listed companies decreased to only 175 by 2019.<sup>662</sup> Academic commentators argue that this significant trend is attributable to the strict and complicated disclosure regime.<sup>663</sup> Another potential reason why listed companies are choosing to delist is

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<sup>656</sup> Law No. 22 of 2015 annulled the previous provisions of the Law No.2 and 3 of 2011 which regulated the disclosure regime of listed companies.

<sup>657</sup> Emiliós Avgouleas, 'What Future for Disclosure as a Regulatory Technique?' above (n 641) 2. See also Mohammad Al-Wasmi, above, (n 428) 207-222.

<sup>658</sup> Abdullāh AlHayyan and Moahamad AlMuatari, above (n 68) 501.

<sup>659</sup> Mathfar Farghali *The Criminal Protection of Trust in the Capital Market: Financial Crime*, (Dar AlNatha Al-Aarabya 2006) 26.

<sup>660</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis' above, (n 641) 2.

<sup>661</sup> Mohammad Ibrahim, 'Three Reasons Why Companies Are Exiting Kuwait Stock Exchange' *Anadolu Agency* (14 April 2017) <<https://www.aa.com.tr/ar/اقتصاد/ثلاثة-أسباب-نزوح-الشركات-من-البورصة-من-الكويت-796568>> accessed 30 January 2020.

<sup>662</sup> Boursa Kuwait, 'Listed Companies' <<https://www.boursakuwait.com.kw/market-participants/listed-companies>> accessed 30 January 2020.

<sup>663</sup> Abdullah Alshebli, above (n 4) 170.

concern about revealing plans to competitors, which they fear would strengthen the competition and weaken their own market position.<sup>664</sup>

The regulator must know how to use the available market information effectively and apply the best policy to protect the markets. Investors need material, precise, complete and prompt information before making investment decisions. This chapter analyses the disclosure of material information by listed companies in Kuwait. It aims to investigate the adoption of a risk-based approach to regulation as a means to protect market integrity. It treats the disclosure of material information as one of the precautionary measures necessary for market protection.

## **2. The conceptual framework of disclosure**

Understanding the importance of disclosure and its relation to the regulator's goals in the financial sector is necessary for the design of a coherent regulatory framework. Inadequate disclosure and disclosure limitations are considered to be among the causes of the 2008 financial market collapse.<sup>665</sup> One of the key issues is whether disclosure is supplying adequate information about stock market risks so as to alert the supervisory authority.<sup>666</sup>

There are two different types of disclosure: disclosure to the regulator and disclosure to the market. Disclosure to the regulator helps it to focus its scarce resources on the most critical stock market risks. The disclosed information gives an insight into a company's performance and, by extension, provides the regulator with a big picture of the market. Disclosure also increases market efficiency, as the disclosed information is used to understand and interpret the foundations underlying stock markets.<sup>667</sup> This allows the regulator to analyse securities information more effectively<sup>668</sup> and reduces the amount of wasteful duplication of market information that participants use to navigate the stock market.<sup>669</sup> Ultimately, the overall costs

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<sup>664</sup> *ibid* 225. Fahad Al-Zumai, 'Protection of Investors in Gulf Cooperation Council Stock Markets: A Case Study of Kuwait, Bahrain and United Arab Emirates' above (n 70). The audience at these workshops highlighted this point during the CMA's workshops on 7 December 2015 and 27 September 2016.

<sup>665</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above (n 641) 205.

<sup>666</sup> FSA, 'The Turner Review, A Regulatory Response to the Global Banking Crisis' (March 2009) available at <<<< [http://www.actuaries.org/CTTEES\\_TFRISKCRISIS/Documents/turner\\_review.pdf](http://www.actuaries.org/CTTEES_TFRISKCRISIS/Documents/turner_review.pdf) >>>> 22 January 2020

<sup>667</sup> Cristian J Meier-Schatz, 'Objectives of Financial Disclosure Regulation' (1986) 8 *Journal of Comparative Business and Capital Market Law* 219, 223.

<sup>668</sup> *ibid* 229.

<sup>669</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' above, (n 12), 1566. See also Cristian J Meier-Schatz, 'Objectives of Financial Disclosure Regulation', above (n 667) 218.

of information retrieval and analysis are reduced when all companies publish standardised financial statements and make these available to local and foreign investors.<sup>670</sup>

Other purposes of disclosure are the protection of investors, the improvement of corporate governance and the positive effect it has on broader public policies.<sup>671</sup> Disclosure gives investors equal access to the information that forms the basis for investment decisions.<sup>672</sup> It is not always clear whether disclosure to the market provides adequate information to protect investors.<sup>673</sup> Policymakers must consider two elements to secure an effective disclosure regime.<sup>674</sup> First, does the disclosure prevent fraudulent practices in the market? And second, does disclosure serve as an adequate tool for regulatory supervision and the protection of the market and its participants? These questions determine the effectiveness of the disclosure regime in both developed and developing countries. There is a general consensus that developed stock markets possess a sufficient standard of disclosure.<sup>675</sup>

In terms of investor protection, Coffee argued that disclosure has two beneficial effects for ordinary investors.<sup>676</sup> Firstly, disclosure enables investors to minimise the variance in their investment portfolios by encouraging them to purchase negatively covariant securities to achieve diversified portfolios. In other words, it gives ordinary investors more options and choices to spread their investments between different portfolios. Secondly, the disclosed information allows investors to estimate better the portfolio value of individual securities.

The questions are how the disclosed information fills the gap between the desired information and the information provided, and how the regulator and investors interpret disclosed information to understand the markets. Theoretically, the disclosure regime gives market actors the necessary amount of investment information to adjust their decisions and strategies, thereby allowing markets to self-regulate.<sup>677</sup> However, whether or not market actors use all the

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<sup>670</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above (n 641). 5.

<sup>671</sup> Cristian J Meier-Schatz, above (n 667) 219.

<sup>672</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' above, (n 12) 1568.

<sup>673</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above, (n 641) 2.

<sup>674</sup> Cristian J Meier-Schatz, above (n 667) 221.

<sup>675</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' (n 12) 1565.

<sup>676</sup> John C Coffee, 'Market Failure and the Economic Case for a Mandatory Disclosure System' (1984) 70 Virginia Law Review 717, 747.

<sup>677</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above (n 641). 2.



available disclosed information to make their investment decisions is open to dispute. The 2008 financial crisis showed how market self-regulation was flawed, and incapable of providing adequate disclosure to alert the regulator about the upcoming crisis.<sup>678</sup> It demonstrated that market participants have limited understanding of disclosed information due to the complexity of financial information. Another factor indicating that investors have limited understanding of disclosed information is that they usually tend to follow trends in the market, which in turn often means failing to make their investment decisions based on disclosed information.<sup>679</sup> In other words, investors ignore the information disclosed by listed companies and followed a ‘herd strategy’ in the market.<sup>680</sup>

All these factors led policymakers to reform policy so as to improve the quality of disclosed information rather than the quantity. The question is how the CMA regulates disclosure to achieve investor protection and market efficiency.

According to the 2015 Executive Bylaws, there are several types of disclosure in Kuwait.<sup>681</sup> The first is preliminary disclosure, i.e. disclosure made before a company is listed on the stock market. The second is periodic disclosure, whereby a listed company discloses information on a regular basis. The third is immediate disclosure, which is necessary when unexpected events or data affect the stock market value of a company.<sup>682</sup> The latter type of disclosure compels a listed company to disclose material information and reveal any risks that could potentially result in company gains or losses.<sup>683</sup> This disclosure takes the form of an immediate, irregular, non-periodic report. It occurs when a significant event is likely to have an impact on companies’ trading prices in the securities market.<sup>684</sup> Sometimes this significant event might be based on information, such as a government agreement or court judgment about a listed

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<sup>678</sup> Ibid 3.

<sup>679</sup> Ibid 12.

<sup>680</sup> Emiliós Avgouleas ‘What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis’, above, (n 641) 12

<sup>681</sup> CMA Executive Bylaws.

<sup>682</sup> Jalal AlOthman (n 544) 125.

<sup>683</sup> Jill F Solomon, Aris Solomon, and Simon Norton, ‘A Conceptual Framework For Corporate Risk Disclosure Emerging from the Agenda for Corporate Governance Reform’ (2000) 32 *The British Accounting Review* 447, 449.

<sup>684</sup> Jalal AlOthman (n 544) 272.

company that all investors should be aware of when making investment decisions.<sup>685</sup> The timing of the announcement of such information is critical in the stock market.

Listed companies need to follow certain general principles when disclosing information. The information must be correct and complete, and may not include misleading statements.<sup>686</sup> Before 2015 the regime in Kuwait relied on listing rules and disclosure rules to control the disclosure of information.<sup>687</sup> The amendments to the 2015 Executive Bylaws modified earlier regulations and introduced a new legal framework for the disclosure regime. Notwithstanding, the CMA has a strict but unpublished policy to oblige listed companies to disclose material information. This was adopted after the 2008 financial crisis to ensure that the regulator is informed about the status of the markets. This unwritten policy was confirmed by Participant No. 2, who played a major role in the CMA:

There is a huge development in terms of disclosure regulations. The listed companies are more aware about the importance to disclose information in the stock markets. The CMA adopts a strict strategy to enforce any breach of disclosure regulation, especially after the issuance of a financial penalty in the 2015 amendments and applying it effectively to ensure that companies know the effect of not disclosing important information.

The next matter to be addressed is what constitutes material information in Kuwaiti stock markets. Here, two issues are tackled. First, does the new regulation provide for a method of assessing disclosed information? Second, can a risk-based approach improve the regime managing the disclosure of material information? The discussion analyses the framework of the disclosure regime in Kuwait in terms of timing of disclosure, type of disclosure, insider lists and form of disclosure.

### **3. Definition of material information**

There has been confusion and misunderstanding between material information and inside information, especially before the issue of the CML amendments in 2015. The law did not

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<sup>685</sup> Humam Alqussi, 'The Legal Framework for Inside Information in Securities Markets: Comparative Study Kuwait and Syria' (2013) 37 Kuwait University Law Journal 427.

<sup>686</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 19 February 2020

<sup>687</sup> Rule No.2 of 2011 listing rules and Rule no.3 of 2012 disclosure rules. See Abdulla Alshebli (n 4) 138. Fatemah Shuraian, above (n 4)

distinguish between the two, and most studies highlight this point.<sup>688</sup> The 2015 amendments define these terms: material information is information that listed companies are obliged to disclose in stock markets, while inside information is unpublished information that insiders use to trade unfairly. This differentiation is important in imposing effective regulation to tackle and prevent insider trading.

The CMA uses a narrow approach to define material information in stock markets, because it is linked only to prudent investors. Material information is defined as:<sup>689</sup>

any information concerning a Listed Company, Listed Fund, Issuer or Obligor, as the case may be, relating to its activity, a person, its financial position or its management which is not available to the public and which relates to its assets, liabilities, financial position or general course of business, which may lead to a change in the price or volume of trading in a relevant Listed Security, or affect the willingness or unwillingness to acquire or divest an interest in such a Security, or may affect the Issuer's ability to meet its obligations.

To identify material information, the listed company must recognise the significant effect of the information in the stock markets. The significant effect is defined as:<sup>690</sup>

information on a transaction, contract or action taken into account when a *prudent investor* makes an investment decision regarding the sale or purchase of Securities, which if announced to the public, may lead to an abnormal change in the price or trading of such Securities.

The CMA uses the prudent investor test to determine the significant effect of material information without giving any definition or clarification of this term. It seems that the CMA uses a strict approach to define material information, requiring that investors must be prudent, which has a bad influence on disclosure of important information.<sup>691</sup> It does not protect the ordinary investor, who is most likely to be affected by material information, unlike the prudent investor who has the knowledge to analyse the markets. This link with prudent investors decreases the amount of information that listed companies must disclose. The interviews revealed that the 'prudent investor' test is a weakness in the disclosure regime, as it will protect only expert investors and not any ordinary investor.

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<sup>688</sup> Samer Abdulllah, 'Preventing using Inside Information in Stock Markets According to Law No.7 of 2010 regarding the establishment of Capital Markets Authority' (Master Dissertation, Kuwait University 2015) 88,147. See also Abdulllah AlHayyan and Moahamad AlMuatari, above (n 68) 90.

<sup>689</sup> CMA Executive Bylaws Module One, Glossary.

<sup>690</sup> *ibid.*

<sup>691</sup> Abdulllah AlHayyan and Moahamad AlMuatari, above, (n 68) 94.

The lack of clarity and links to a prudent investor hinder the application of an effective disclosure regulation. It is difficult to determine what would constitute ‘material information’ in the Kuwaiti market. Effective regulation requires an informed industry that possesses an understanding of the environment in which the law will be applied.<sup>692</sup> When regulating the Kuwaiti market, the CMA must also consider the culture of compliance and the overall expertise of industry actors.

The seven expert interviewees noted this narrow approach to link material information to prudent investors, but Participant No. 5 justified the approach as being part of the CMA policy to adopt strict financial regulation:

In terms of the prudent investor as stated in the bylaws, it is important to understand the regulator’s philosophy when issuing the CMA law. Is it a strict or flexible policy? Most jurisdictions adopt a flexible policy, but in contrast Kuwait has adopted a strict policy regarding the disclosure regulation. The Executive Bylaws stated that the information must impact a prudent investor not an ordinary investor. In fact, it is a very judgemental decision to make. Therefore, the law requires that the information must impact the prudent investor to protect the listed companies from rumours. Furthermore, the impact of the information on an ordinary investor might be temporary and will disappear after a while, so we cannot drag the listed company by this unstable impact that might even be a rumour. On the other hand, the prudent investor has the experience to understand the markets and the impact of material information on the stock markets. Therefore, a listed company should disclose this information immediately to tackle insider dealing. The impact of material information on a prudent investor will continue not on a temporary basis, so it is a strict policy to protect the markets from any rumours and general discussions on social media.

The other six participants disagree with this statement, as it is a way to limit disclosure power to prevent insider trading.

Participant No. 1 stated:

I believe that the articles about the prudent investor were added in the final 2015 CMA amendments. Which, no doubt, reduces the amount of announcements, which reflects the transparency of the market in a direct way. So when we connect material information with its effect on the prudent investor, we then decrease the amount of announcements in the market. As we know, not all investors are experts.

Participant No. 2 said:

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<sup>692</sup> Julia Black, *Rules and Regulators* (n 446) 12.

Honestly, I am not familiar with the prudent investor test that the law stated. If this is the case, it means that this provision might be added without sufficient study of the markets: it narrows the disclosure effect to a certain type of investor, which does not cover the majority of Kuwaiti investors. To be clear, most investors are ordinary, either retired or non-specialists

Participant No. 3:

Indeed, unclear definitions of inside and material information confuse companies on what is required to be disclosed, especially when there are no advisory firms for consultation. In terms of material information with the prudent investor, is a violation of the law. In addition, it does not serve its main purpose, which is to protect the regular investor. In fact, this information should influence the decision-making of the regular investor, to enable his/her protection. I believe that this provision is illegitimate and unconstitutional, as it violates the Executive Bylaws and is absent from the superior law that mentions the connection between the information and the prudent investor. In fact if the CMA refers me to the prosecutor based on this provision, I will file a petition to annul this provision. The CML is the superior law over the bylaws, which means that the bylaws should not create or issue a new provision without clear authority to allow this delegation. This provision regarding linking the influence of inside information with prudent investors is clearly illegitimate.

Participant No. 4:

The purpose of disclosures is to provide equal opportunity for all investors to get useful information, while protecting them, especially non-experts. Moreover, the connection of material information to prudent investors would be confined to only a small category of investors, which is the opposite of what the law was made for.

Participant No. 6:

It is impractical to link material information with prudent investors, because this information affects ordinary investors who are mostly retired and old people who trade in stock markets. Additionally, the law did not clarify the level of prudence, if it is an expert person or a person with experience or an educated one. A lot of listed companies have contacted the Disclosure Department to ask about material or inside information and how it affects prudent investors. There is no coherent system to direct the companies to the right department, it is like a maze. For example, a listed company asked the disclosure department at the CMA if they should disclose or enter a verdict against them to pay 5,000 Kuwait dinars which is a fine against the company. This information is not material because the amount of fine is low in comparison to the company's capital. It depends on the listed company itself: in some cases the same judgment amount will be material information that needs to be disclosed if the company has little capital. For example, if National Bank of Kuwait loans or borrows 1 million it is not considered material information because its capital and business value exceed this

amount, but if the company has lower capital then this information is material and needs to be disclosed. The prudent investor test does not help to clarify the concept; it did the opposite, as listed companies avoid the disclosure of material information because it does not affect the prudent investor test.

Participant No. 7:

It does not help the judges to punish the listed companies for not publishing material information. It is a very strong argument to state that this unpublished information does not affect a prudent investor, so they do not have to announce it. The CMA must reform its policy to protect the ordinary investor.

The 2015 Executive Bylaws provide more detail: they define material information and provide 29 examples of what constitutes such information,<sup>693</sup> but state that the understanding of the notion of material information is not limited to the examples offered. They also state that ‘disclosure shall be made for any changes that result in a significant increase or decrease in the assets, liability, income or expenses of a listed company’. Some jurisdictions take further steps and require that for definitional purposes all information must be specific and precise.<sup>694</sup> Such rules are welcome, as disclosure regimes should be unambiguous and indicate in precise terms the required information so as to protect investors and market participants.<sup>695</sup> For this reason, the researcher believes that the CMA must adopt new policies and issue clear statements about material information to give a more rational approach, like a ‘reasonable investor’ test. Even with the examples included in the Executive Bylaw amendments in 2015, policy statements and clarification would help to ensure that listed companies are aware of the importance of the disclosure of material information.

In contrast, the FCA does not use the term ‘material information’ to refer to listed companies’ obligations to disclose inside information. The FCA regulates these obligations to disclose inside information through Disclosure Guidance and Transparency Rules.<sup>696</sup> The FCA defines inside information that must be disclosed in a clear sense, including its precise nature, and applies a ‘reasonable investor’ test to determine the influence of inside information on market

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<sup>693</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4.1.

<sup>694</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 13 March 2020.

<sup>695</sup> Cristian Meier-Schatz (n 667) 221.

<sup>696</sup> DTR Disclosure Guidance and Transparency Rule, FCA Handbook’ available <<https://www.handbook.fca.org.uk/handbook/DTR/2/2.html>> accessed 13 February 2020

prices.<sup>697</sup> This means that a company should make its assessment of what information to disclose based on how it thinks a reasonable investor would act on this information.<sup>698</sup> The FCA provides guidance on the reasonable investor requirements to ensure that listed companies can understand the definition of the test.<sup>699</sup> The UK courts also use a ‘reasonable investor’ test to determine whether information is inside information.<sup>700</sup> There is no percentage change or figure that constitutes a significant effect on a company’s shares in the stock market,<sup>701</sup> and the FCA discourages listed companies from using the ‘10 per cent rule’ to define inside information<sup>702</sup> because shares in a small listed company will be more volatile than those of a large listed company.<sup>703</sup> The FCA sets out a provision to distinguish inside information from rumours: the information must be precise.<sup>704</sup>

This analysis demonstrates that Kuwaiti laws lack precision and guidance on what constitutes material information. The prudent investor test is too strict, and relies on a knowledge of listed companies to determine the effect of information on prudent investors. In addition, Article 4.1.1 of the Executive Bylaws states that ‘the Board of Directors of a Listed Company shall disclose its assessment of the expected effects of such material Information on its financial position, excluding the effects that cannot be foreseen or measured’.<sup>705</sup> The critical problem with this provision is that it lacks clarity. The examples provided in a guidance section refer to events that may affect listed companies or circumstances in which they may find themselves. In most cases, however, the events are unique, as listed companies face new events and challenges every day. There are no published guidelines to help companies understand the underlying rules and regulations.

A listed company’s concealment of or failure to identify material information through the implemented disclosure regime constitutes a breach of the CML.<sup>706</sup> However, there is no policy

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<sup>697</sup> DTR 2.2.6 available at ‘DTR 2.2 Disclosure of inside Information - FCA Handbook’ <<https://www.handbook.fca.org.uk/handbook/DTR/2/2.html>> accessed 13 February 2020. See also Raghda Al-Qatanani, above (n 260) 83, 140-141

<sup>698</sup> Ibid., DTR 2.2.5 - 2.2.6

<sup>699</sup> Brain McDonnell, *Inside Information: A Guide to the Disclosure Rules* (2nd edn Sweet & Maxwell, 2013) 7

<sup>700</sup> Section 118(c) 6 of FSMA. See also Barry Rider, Kern Alexander, and Lisa Linklater, *Market Abuse and Insider Dealing* (Tottel, 2007) 46.

<sup>701</sup> DTR 2.2.4, See also Brain McDonnell, above(n 699) 8

<sup>702</sup> Brain McDonnell, above, (n 699) 8.

<sup>703</sup> Brain McDonnell, above (n 699) 8.

<sup>704</sup> FSMA s. 118(C).

<sup>705</sup> CMA Executive Bylaws, Module 10, Chapter 4, Article 4.1.1

<sup>706</sup> CML, Article 120 and 121.

on how the CMA Disclosure Department identifies inaccurate material information. In practice, the Disclosure Department follows a company's news online and in print to ensure that disclosure reflects the company's performance. It is worth noting that CMA staff rely on their judgement to identify inaccurate information; there is no internal policy to verify a disclosure statement. As Participant No. 6 confirmed, there is no training programme to teach the CMA Disclosure Department how to identify incorrect disclosure.

#### **4. Procedure for the control and disclosure of material information**

The creation in the 2015 amendments of a method for releasing or disclosing material information is a good development in the Kuwait disclosure regime.<sup>707</sup> The procedures and requirements for releasing material information using this method are clearly outlined.<sup>708</sup> It is paramount that the system is secure and reliable, otherwise disclosure is meaningless. Previously, the CMA was criticised for failing to adopt a standard procedure for disclosing material; this affected market competition because some listed companies disclosed their information prematurely, and in doing so revealed their commercial strategies.<sup>709</sup>

Furthermore, a listed company is obligated to take precautions to limit the potential misuse of inside information.<sup>710</sup> It must take adequate steps to disclose material information that are proportionate to the company's nature and its type of business. Disclosure of material information by a listed company should take into account several factors, discussed below.

##### **4.1 Who should determine the nature of material information?**

The regulator compels listed companies to disclose material information to ensure that all investors have equal access to the data required to make informed investment decisions. The disclosed information should be objective, consistent and accurate.<sup>711</sup> A listed company must determine what kind of information should be considered material and disclosed immediately.<sup>712</sup> In particular, the board of directors of a listed company is responsible for assessing the data and making a decision about which information should be disclosed. The

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<sup>707</sup> CMA Executive Bylaws.

<sup>708</sup> CMA Executive Bylaws, Module 10, Chapter 4, Article 4-6.

<sup>709</sup> Abdullah Alshebli (n 4)150.

<sup>710</sup> CMA Executive Bylaws, Module Ten, Chapter Three, Article 3-2-1.

<sup>711</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 19 February 2020.

<sup>712</sup> *ibid*, Module ten, Chapter Four, Article 4-1-1, 4-2.



directors are in the best place to assess the company's data to decide if information is material or not.<sup>713</sup> The issuer – which any a corporate entity entitled to issue securities<sup>714</sup> – is required to disclose material information to the CMA and the KSE Boursa before releasing the information to the public. For example, on 17 January 2019 the CMA fined the Asia Capital investment company 2,000 Kuwaiti dinars (approximately £5,000) for failing to file a disclosure simultaneously to the CMA and Boursa.<sup>715</sup> A listed company undertakes full responsibility for deciding what kind of information to disclose, and is liable for the consequences of its decision.<sup>716</sup>

One critical development in the 2015 Executive Bylaws was the introduction of provisions making listed companies accountable for their own disclosed information.<sup>717</sup> This is a step closer to adopting a risk-based approach to disclosure, which would ensure that CMA interference with listed companies is minimal. This approach resembles the UK model, where the FCA decided that the issuer and its advisers should make a first assessment of the nature of information.<sup>718</sup>

As determining the nature of material information is a complex task requiring case-by-case assessment, the CMA's Disclosure Department adopts an open-door policy to discuss with listed companies what information should be disclosed.<sup>719</sup> As mentioned, this approach has faced some criticism, but in principle it is a good practice that ensures ongoing dialogue with the industry, mainly because the CMA does not recognise the authority of advisers in determining material information.

To put this in comparative perspective, when determining the nature of material information the UK FCA allows a listed company to take professional advice from financial advisers,

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<sup>713</sup> Brain McDonnel, above (n 699) 5.

<sup>714</sup> CMA Executive Bylaws Module One, Glossary

<sup>715</sup> CMA, 'Statement' 'الهيئة إصدارات - المال أسواق هيئة' <<https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/642095>> accessed 18 March 2020.

<sup>716</sup> CML, Article 107.

<sup>717</sup> CML, Article 107.

<sup>718</sup> DTR 2.2.7 available at 'DTR 2.2 Disclosure of inside Information - FCA Handbook' <<https://www.handbook.fca.org.uk/handbook/DTR/2/2.html>> accessed 18 March 2020.

<sup>719</sup> The CMA's workshop on 26 September 2016 about 'Material Information and the Methods of their Disclosure'. The Speakers are: Amro AlMuharib; Director of Disclosure Department, Jassim Aldrees; Manager of Material Disclosure Section, Khalid Alsager; Director of Awareness office, and Othman Alneghaimesh: Director of Co-ordination & Follow up Office Legal Affairs Sector available at <<https://www.cma.gov.kw/ar/web/cma/home>> accessed 18 March 2020.

auditors and lawyers.<sup>720</sup> However, the FCA holds that listed companies cannot fully rely on the opinions of advisers to decide on material information, as the ultimate responsibility for determining what constitutes material or inside information rests with the company.<sup>721</sup> For example, in 2009 the former financial regulator (the FSA) fined Wolfson Microelectronics £14,000 for delaying disclosure of inside information, even though the delay was based on an advisory opinion.<sup>722</sup>

#### 4.2 Disclosed information

Disclosure is insufficient where it does not provide enough information about the company's performance. A listed company may fulfil its obligations to disclose material information, but this disclosure does not achieve the purpose of the rule. For example, in February 2017 Agility, which is company listed on Kuwait's stock market, made insufficient disclosure about its investments in Iraq.<sup>723</sup> Investors were surprised that the Agility disclosure contained minimal information about the company's Iraqi investments although there were significant events in Iraq. After investors raised their concern about the company's insufficient disclosure in the press, the CMA stopped trading of Agility shares in the stock market on 20 February 2017.<sup>724</sup> This example shows that the quality of information disclosed may not provide enough information to investors, thus further reform is needed to ensure that disclosure includes enough information about a company's status. The UK FCA requires listed companies to take all reasonable care to ensure that information is not false, misleading or deceptive,<sup>725</sup> and sets out a framework to ensure that disclosed information is of sufficient quality and reflects the company's performance. The lack of quality in disclosure by Kuwaiti listed companies might lead to financial crisis and difficulties. The interviews confirmed that insufficient disclosure is a weakness and does not reflect company performance.

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<sup>720</sup> DTR 2.2.7, 'DTR 2.2 Disclosure of inside Information - FCA Handbook'

<sup>721</sup> *ibid.*

<sup>722</sup> The FCA 'Final Notice - Wolfson Microelectronics Plc' <[https://www.fca.org.uk/publication/final-notices/wolfson\\_20jan09.pdf](https://www.fca.org.uk/publication/final-notices/wolfson_20jan09.pdf)> accessed 18 March 2020.

<sup>723</sup> Tamer Hamda, 'Agility Investors are requesting for more transparency' (2017) <<<https://alqabas.com/360133/>>> accessed 18 March 2020.

<sup>724</sup> *ibid.*

<sup>725</sup> DTR 1.3.4R 'DTR 1.3 Information Gathering and Publication - FCA Handbook'

The 2008 financial crisis proved that an uninformed regulator is unable to protect the markets;<sup>726</sup> there is nothing worse than a vague and ill-informed industry. Listed companies provide minimum information, which means they have fulfilled their obligations, but at the same time the Kuwaiti regulator and investors are unaware of the true picture. As Participant No. 4 clarified, listed companies do not explain the impact of disclosed material information on the stock markets. It is important to reform the current regime to give enough information to market participants. The CMA should issue guidance and clarification setting out the minimum information to be disclosed. Listed companies need to understand the underlying policy of disclosure objectives. It is extremely important that the CMA takes immediate action to reform the quality of disclosure.

Another important element is the absent of policy and procedures to check the accuracy of a listed company's disclosure. The CML and its Executive Bylaws do not state the method for checking a company's disclosure. The interviews confirmed this as a weakness in the CMA. In addition, there is no legal obligation on the CMA to follow up incomplete or inaccurate disclosure – the CMA may or may not request further clarification. This affects even the accountability of the CMA to ensure the accuracy of disclosed information. As the CML does not place any obligations on the CMA in this regard, it can neglect disclosure without any accountability. Participant No. 4 confirmed that the CMA must be obliged to instruct a listed company to complete and clarify any incomplete or inaccurate disclosure. In fact, the interviews revealed that listed companies approach the CMA Disclosure Department to inform it about inaccurate disclosure by other companies. This shows weaknesses in the CMA procedures to ensure that disclosure is accurate. It is suggested that the CMA should adopt a policy with clear procedures to check the accuracy of listed companies' disclosures.

The researcher asked the interviewees about their opinion of the CMA role in checking the accuracy of disclosed information.

Participant No. 6 stated:

There is no policy or procedure to check the accuracy of disclosed information and its quality. It depends on the employee's knowledge and connections. Sometime the Disclosure Department learns about inaccurate information from the newspapers or online resources. For example, some listed companies

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<sup>726</sup> Emiliós Avgouleas, *Governance of Financial Markets: the Law, the Economic, the Politics* (Cambridge University Press, 2012) 2, 22, 26.

contacted the CMA department to provide information about other listed companies for violations of disclosure regulation and accusing the CMA of applying punishments and penalties randomly. There is no policy to request these companies to provide further clarification. It depends on company's reputation, and if it has previously committed any violation or crime, the Disclosure Department will ask the company to provide more answers and clarification. Another example: a family listed company disclosed that they bought real estate without clarifying the buyer's name and it appeared that the buyer was related to one of the board members of the company, so it might not be a good investment.

Participant No. 2 said:

The CMA is not responsible for checking the disclosed information. If it appears that the disclosed information is incorrect, the CMA imposes penalties. There is no clear policy to check the accuracy.

Participant No. 3 said:

The CMA supervises the disclosure, and if they found any false information they will investigate. Needless to mention that there could be manipulation in terms of the value of the disclosed information. In some cases the information is minimal, which does not really reflect the performance of the company.

Participant No. 4 stated:

The disclosure mechanism is inefficient. If the disclosure or the announcement is vague or incomplete, the CMA or Boursa 'may' instruct the company to provide more information to clarify or complete the disclosure. The CMA or Boursa 'must' instruct the company to provide such clarification. The law must in turn be amended to allow the mentioned authorities the power to request further details and clarifications regarding the announcements. The regulatory authorities must be obligated to ensure that disclosures fulfil all the requirements stated by the law to be clear and complete, etc.

Another critical differentiation between the UK and Kuwaiti systems is that the FCA requires justification for the disclosure decision; this helps to clarify the links between the material/inside information and the company's share value in the stock market. The CMA does not require justification for the disclosed information. The CMA needs to reform the disclosure obligations for listed companies to provide further justification for disclosures made in the stock market. Currently disclosures made by listed companies do not show the link between the disclosed information and the company's share value. Reforming the quality of disclosed information will have a positive effect on the information available for market participants and companies' share values. At present, investors in Kuwait cannot analyse disclosed information to make an investment decision. Academic commentators criticise the lack of clarity in the

current regime, as the disclosures are short, vague and unjustified.<sup>727</sup> The interviews held differing views about the lack of clarity and inadequacy of some disclosures: of the seven experts, four felt there is insufficient information to reflect company performance, while three felt the information is enough but investors do not have the knowledge to analyse it. This disagreement on the clarity of disclosure in stock markets reflects the sensitive positions the interviewees hold in the financial system: they will not admit the shortcomings in listed companies' disclosures. The reality and practice show that current disclosure does not provide enough data to give equal access to information. It needs further reform to ensure that disclosure presents quality information and reflects a company's performance in the markets.

Participant No. 1 stated:

I believe that the current disclosure provides enough information for investors about the company's performance. In return, investors and individuals must analyse and understand the disclosed information. They need to have the proper awareness to properly understand the disclosures. The CMA is not responsible for checking the disclosed information. If it appears that the disclosed information is incorrect, the CMA must impose penalties.

Participant No. 3 said:

The disclosure of information by listed companies in stock markets is important. The CMA punishes non-compliant companies to ensure understanding of the importance of disclosing inside information and to deter any illegal action from other companies as well.

Participant No. 5:

The markets need time to understand inside information and it is necessary to increase awareness about the material information to be disclosed in the stock markets. In fact, the Executive Bylaws explain the material information in detail and provide examples about material information as well, to ensure that listed companies disclose the right information.

The other four interviewees felt that the disclosure regime is insufficient.

Participant No. 2 said:

The application or enforcement of the disclosure regulation must be further developed. The written law is effective, but in reality and application it is not. For example, the disclosure regulation requires listed companies to disclose any losses that exceed 75 per cent of their capital and stop their stock from trading in

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<sup>727</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 466.

the stock markets. The listed company only announces their annual loss, without mentioning the percentage against the company's capital. The CMA discovered this practice after a company lost 102 per cent of their capital and the CMA did not know about it. It led the CMA to amend the law to obligate listed companies to submit their financial statements for auditors to review and approve. The CMA's role is to ratify the approval without going in details. To be honest, this current structure of disclosure does not provide enough of the information that is needed for further development.

Participant No. 4:

Current disclosure statements are extremely bad. They do not provide information about the influence or the impact of the disclosed information at all. Most disclosure statements show no financial impact of the disclosed information. If that's the case, then why is the company disclosing information if there is no financial impact? It means that listed companies and the CMA do not understand the purpose of the disclosure regulation and what should such disclosure achieve. An obvious example of unclear disclosure was by Kuwait Gulf Link Transport Company (KGL), one of the listed companies, when they announced a court judgment on their favour, by the court affirmation of provisions 1 and 2, without any clarification regarding the content of the provisions nor their effects on the company. In addition, neither the CMA nor the Boursa (stock market) requested any clarification from the company, which is indeed unacceptable. The CMA must oblige companies to provide further details on their announcements. And in case of failure to do so, the CMA is then held accountable.

Participant No. 6:

Most announcements are insufficient because they do not provide clear and sufficient information about the impact of disclosed information. For example, a listed company disclosed that they bought a real estate and it cost 1 million Kuwait dinar. The questions are as follows; is this real estate located in Kuwait or abroad? Is it in a good location? Is this real estate a rental building that will provide monthly income? All these questions need to be answered to allow the investor to evaluate if this is a good or bad investment.

Participant No. 7:

The CMA obligates the listed companies to publish a lot of information; some disclosures have only minimum information.

At a CMA workshop on 'Material Information and the Methods of Its Disclosure' on 26 September 2016, CMA officials stressed the importance of immediate disclosure of material information.<sup>728</sup> This was the subject of a heated discussion, with one member of the audience

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<sup>728</sup> The CMA's workshop on 26 September 2016 about 'Material Information and the Methods of their Disclosure'. Above (n 719)

asking about the criteria to determine material information. The official replied that this would be up to the issuer to determine, without offering any explanation or clarification about how a listed company would determine the influence of information on investors. This debate is not new; academic commentators have raised concerns about the effects of this unclear standard on price information and trading securities.<sup>729</sup> Even after the issue of the Executive Bylaws in 2015, reforms are still needed to clarify the definition of material information.

Furthermore, discussions at this workshop<sup>730</sup> demonstrated that the CMA has an open-door policy, meaning that its Disclosure Department is prepared to consult with a listed company about whether information should be disclosed or not. Although this is a good practice, the CMA does not record such consultations or confirm the content of the discussion and its conclusions. In other words, there is no evidence trail to indicate that a listed company has communicated with the CMA Disclosure Department.<sup>731</sup> This is another crucial issue the researcher believes the CMA should consider. The CMA should engage in quality dialogue with the market and its participants. Notably, one of the reasons for the collapse of Northern Rock in 2008 was a lack of communication between the FSA and the firm.<sup>732</sup>

Insufficient communication weakens the supervisory abilities of the regulator; hence clear standards governing the open-door policy must be adopted to protect both the listed companies and the CMA. If an employee of the CMA Disclosure Department states there is no need to disclose certain information, but uses the information for self-interested purposes or shares the information with another company, the interests of the listed company are unprotected. The employee might be sanctioned for violating the Code of Conduct, but the listed company will be harmed. In short, an open-door policy must be structured in such a way as to protect listed companies.

Determining the nature of material information is the first step in the application of the risk-based approach. The legal framework for disclosing material information helps in the

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<sup>729</sup> Ahmed AlMulhem, above (n 9 ) 15. See also Adel AlManea above (n 9 **Error! Bookmark not defined.**) 19. and Abdullah Alshebli (n 4 **Error! Bookmark not defined.**) 226.

<sup>730</sup> The CMA's workshop on 26 September 2016 about 'Material Information and the Methods of their Disclosure'. Above (n 719)

<sup>731</sup> The CMA workshop (n 719) The audiences raised a question regarding the communication with the CMA Disclosure Department at the CMA, pointing out that there is no evidence from the CMA to confirm the communication.

<sup>732</sup> David Bholat, James Brokes, Chris Cai, Katy Grundy and Jakoob Lund, above, (n 76)

assessment of risks. A listed company can also employ the risk-based approach to assess material information. This entails focusing on a risk disclosure strategy to avoid engaging in action that might harm or otherwise negatively affect the company. If a company uses a risk-based approach and discloses risk, it will prevent speculative reports that might harm its objectives. Hence the risk-based procedure relies on the effectiveness of company's internal management and places responsibility on the company.<sup>733</sup> More specifically, the senior management of the company are normally liable for decisions regarding disclosure requirements. The risk-based approach dilutes the burden on regulators by requiring listed companies to develop their own compliance systems and demonstrate their compliance to the regulator. This approach is also referred to as management-based regulation, meta-regulation or enforced self-regulation.<sup>734</sup> There are three main areas that a company should improve if it is to secure an effective disclosure system: internal control, corporate risk management and corporate risk disclosure.<sup>735</sup> The risk-based approach can help listed companies in Kuwait to be compliant and encourages them to adopt policies to assess risk internally and disclose these risks to regulators and market participants. This obliges companies to identify risks and prioritise them accordingly.

The quality of disclosed information is important in achieving an effective disclosure regime, ensuring that all investors have equal access and preventing any use of inside information.

#### 4.3 Timing of disclosure of material information

The schedule for publishing material information is extremely important in tackling and preventing insider trading. The regulations in Kuwait require a listed company to disclose material information immediately,<sup>736</sup> but do not specify the nature of material information. Material information can have either a positive or a negative effect on a company's shares in the stock market.<sup>737</sup> The CMA and Boursa are required to announce the disclosure of material information during working hours. If the stock market is closed, the CMA or Boursa must announce the information 15 minutes prior to the start of the next trading session.<sup>738</sup>

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<sup>733</sup> Julia Black, 'Regulatory Styles and Supervisory Strategies' (n 446) 226.

<sup>734</sup> *ibid* 227.

<sup>735</sup> Jill F Solomon, Aris Solomon, and Simon Norton, (n 683) 450.

<sup>736</sup> CMA Executive Bylaws, Module 10, Chapter 4, Article 4-2.

<sup>737</sup> Adel AlManea (n9) 25.

<sup>738</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4-2-1.



When a company is listed on a foreign exchange or market it is regulated in the following way:<sup>739</sup>

if a Listed Company's Securities are listed in a foreign Exchange or market, it takes all the necessary measures to ensure that the disclosure of Material Information is made simultaneously in all such markets. If the regulations of a foreign market require the company to disclose Material Information on a day which is a public holiday in Kuwait, the Company shall immediately disclose the information to the Authority and the Exchange at the latter's opening of the business day and at least fifteen minutes prior to the next trading session of the Exchange in Kuwait.

This research argues that this provision does not offer sufficient protection to investors and market participants. Such a situation is likely to occur frequently, taking into consideration the fact that the weekend in Kuwait falls on Friday and Saturday. Considering modern online news services and instant social media publishing, the possibility of delaying or postponing disclosure is unacceptable. An alternative model of information disclosure, such as the UK's 'weekend disclosure', could be used.<sup>740</sup> The UK Stock Exchange is closed over the weekend, but there is a provision to address this matter: the so-called 'Friday night drop case'.<sup>741</sup> The FCA requires firms to disclose information over the weekend in one newspaper to make the information publicly available.<sup>742</sup> This kind of rule does not exist in the Kuwaiti regime.

Academic commentators criticise regulation that forces listed companies to reveal their plans to competitors.<sup>743</sup> Excessive or overly detailed disclosure by a listed company affects its business and performance.<sup>744</sup> Further, regulation does not allow for a delay in disclosure. Any delay or postponement of disclosure is only permitted in accordance with the law. For example, if a company is engaged in negotiations with the government, this information might affect the company's market price and share value. In such cases the company may ask for a delay or postponement of disclosure to protect the confidentiality of ongoing negotiations.

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<sup>739</sup> *ibid.*

<sup>740</sup> Brain McDonnell, above (n 699)11.

<sup>741</sup> Louise Wolfson, 'Continuing Obligations' in Toby Wallis (ed), *A Practitioner's Guide to the Financial Services Authority Listing Regime, 2012/2013* (Sweet & Maxwell 2012).

<sup>742</sup> DTR 1.3.6R 'DTR 1.3 Information Gathering and Publication - FCA Handbook'

<sup>743</sup> Abdullah Alshebli, above (n4); Fahad Al-Zumai above (n 70).

<sup>744</sup> Luca Enriques and Sergio Gilotta above (n 423).

In cases of irregular disclosure, information must be disclosed in full and no significant omissions are permitted. The conditions and requirements for requesting a delay or postponement of disclosure are detailed below.

#### 4.3.1 Initial disclosure

The disclosure regime requires a listed company to engage in full and accurate disclosure, which means that the disclosed information may not contain misleading or unclear statements or terms that might cause harm in the stock market.<sup>745</sup> Material information must be disclosed in full, and no significant omissions are permitted.<sup>746</sup> The 2008 financial crisis highlighted the importance of complete disclosure to be able to gauge market risks. In 2008, for example, incomplete information regarding the on- and off-balance sheets of banks led to the exposure of structured credit products.<sup>747</sup> The availability of good-quality information for market participants is essential for a strong securities market.<sup>748</sup> Listed companies must not provide incomplete information to investors and market participants.<sup>749</sup>

During the disclosure process, however, some material information might not be available at the time of the relevant trading session, resulting in incomplete information. Listed companies may ask the regulator to postpone disclosure until the information is complete. Under such circumstances the listed company must petition the CMA and Bursa to postpone disclosure and request the temporary suspension of trading in its securities.<sup>750</sup> This is a good practice, because during the 2008 financial crisis market actors failed to understand the risks and prevent a crisis even though companies engaged in full disclosure.<sup>751</sup> Hence temporarily halting trading in securities is preferable to facing unexpected risks.

Apart from this, disclosure regulations require a listed company to announce the reasons for non-disclosure, the temporary suspension of trading and the expected duration of the

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<sup>745</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 18 March 2020.

<sup>746</sup> *ibid.*

<sup>747</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above, (n 641)

<sup>748</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' (n 12 **Error! Bookmark not defined.**) 1565.

<sup>749</sup> IOSCO, 'Principles for Periodic Disclosure by Listed Entities' <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>> accessed 19 February 2020.

<sup>750</sup> CMA Executive Bylaws), Module Ten, Chapter Four, Article 4-2-3.

<sup>751</sup> Emiliós Avgouleas 'What Future for Disclosure as a Regulatory Technique? Lessons from Behavioural Decision Theory and the Global Financial Crisis', above, (n 641)

suspension. Further details should be announced as soon as they are available. Before the 2015 CMA amendments, Bursa had to approve a listed company's request for non-disclosure and temporarily halt trading its shares. Currently it is up to the listed company to postpone or delay disclosure, but if the reasons for this postponement or delay are not proportionate the company will face legal consequences.<sup>752</sup> This uses the risk-based approach to place full responsibility for the postponement or disclosure on the listed company.

#### 4.3.2 Delaying disclosure

In exceptional cases a listed company can delay the public disclosure of material information if it would damage ongoing negotiations or preliminary procedures preceding a deal. The length of delay must be proportionate to the circumstances. Delaying disclosure is not subject to CMA approval.<sup>753</sup> This is a new development, using a risk-based approach and minimising CMA control over listed companies. The ultimate responsibility for the consequences of a delay rests with the listed companies.

The conditions for delaying disclosure are as follows.<sup>754</sup>

- 1) A delay may not be requested for the purpose of issuing misleading information about facts and circumstances that are used to evaluate the listed company's securities.
- 2) The listed company shall take all necessary measures to ensure the confidentiality of material information until the moment of disclosure.
- 3) Subsequent to the disclosure of the material information, the listed company must justify the disclosure delay.

However, if the CMA discovers that the reason for postponing or delaying disclosure was unjustified, it can impose disciplinary sanctions.<sup>755</sup> There are no standards or policies that explain how companies are to determine the nature of the material information or on what basis the CMA will conclude that a delay is justified. This research argues that it is advisable to announce and regularly update policy guidelines concerning delayed disclosure to rectify this

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<sup>752</sup> CMA Executive Bylaws , Module Ten, Chapter Four, Article 4-3-1

<sup>753</sup> *ibid.* Article 4-3.

<sup>754</sup> *ibid.* Article 4-3-1

<sup>755</sup> CMA Executive Bylaws.

lack of regulation. The letter of the law should be adjusted to meet industry needs and legal objectives for the sake of effective enforcement.<sup>756</sup>

In addition, a listed company can consult the CMA before delaying disclosure to determine if a delay is valid.<sup>757</sup> This consultation occurs on a case-by-case basis; the CMA does not provide guidance with regard to this matter.

Academic commentators have suggested two reasons for the trend in listed companies delisting from the KSE: first, the disclosure regime is too strict, and second, disclosure damages listed companies by revealing their plans to competitors.<sup>758</sup> The amendment to the 2015 Executive Bylaws that currently allows the postponement or delay of disclosure helps to ensure that the intentions of listed companies are kept confidential so potential competitors will not profit from early disclosure information, but this amendment did not prevent listed companies from delisting and withdrawing from the KSE. Some listed companies withdraw from the KSE because they have not taken the necessary steps to apply new financial regulation provisions.<sup>759</sup> Other companies delist due to foreign company mergers.<sup>760</sup> The most important factor here is unclear disclosures that lead to unstable trading.<sup>761</sup> In 2017, for instance, there was an unclear disclosure by the Americana Group food company regarding its decision to delist from the Kuwait stock market.<sup>762</sup> This led to rumours and news items about delisting, which had a significant effect since the company's capital is approximately 40.2 million Kuwaiti dinars (about £102 million) distributed in 402 million shares, with a par value of 100 fils per share.<sup>763</sup> The information disclosed by Americana was not sufficiently transparent in explaining the steps the company would take to delist itself from Boursa Kuwait. This incident highlights the importance of including sufficient information in a disclosure to ensure that investors can make investment decisions based on accurate and adequate data.

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<sup>756</sup> Julia Black, *Rules and Regulators* (n 446) 16.

<sup>757</sup> The CMA's workshop (n 719).

<sup>758</sup> Abdullah Alshebli (n 4) **Error! Bookmark not defined.** 225. See also Al-Zumai (n 70).

<sup>759</sup> Al Joman Center for Economic Consultancy, 'Phenomenon of Withdrawal of Companies from Listing on the Kuwait Stock Exchange' (2015) <<http://www.aljoman.net/document.aspx?v=140692&LINK=no>> accessed 19 February 2020.

<sup>760</sup> *ibid.*

<sup>761</sup> Abdullah AlHayyan and Moahamad AlMuatari, above (n 68) 505

<sup>762</sup> Mahmoud Bader, '42 Listed Companies left the Kuwait Stock Exchange During the last 18 Months' (2016) Alarabya newspaper <<https://www.alaraby.co.uk/economy/2016/8/15/42-شهر-18-شركة-تغادر-بورصة-الكويت-خلال>>

<sup>763</sup> Mohamad Farouk, 'Americana Ends 34-yr listing on Boursa Kuwait' *Mubasher* (23 April 2018) available at <<https://english.mubasher.info/news/3269351/Americana-ends-34-yr-listing-on-Boursa-Kuwait/>> accessed 18 March 2020.

## 5. Selective disclosure

In the ordinary course of business a listed company deals with firms and individuals, negotiates agreements and prepares bids. Listed companies do not have a power or legal obligation to forbid third parties such as legal advisers from disclosing material/inside information. Over the course of deals or transactions, the disclosure of information related to a project is referred to as selective disclosure.<sup>764</sup>

Previously, the disclosure regime in Kuwait did not recognise selective disclosure, and this was criticised by scholars.<sup>765</sup> After CMA Resolution No. 2 of 2012, issued with respect to the disclosure of material information, the CMA began to require selective disclosure to prevent leaks of material information on the market. This resolution identified a group of people who could be within the scope of selective disclosure. However, the CMA cancelled Resolution No. 2 of 2012 and replaced it with the Executive Bylaws, hence some scholars have concluded that currently there is no regulation regarding selective disclosure.<sup>766</sup> This research argues that this conclusion is incorrect: selective disclosure is regulated in the provision in the Executive Bylaws for corporate insiders' lists.<sup>767</sup>

Selective disclosure now applies to material/inside information that emanates from 'any other person or entity who is directly linked to the company and holds inside information related to the Listed Company or its clients including, but not limited to, the Parent Company, the Auditor, banking firms, advisory firms, Credit Rating Agencies, information technology companies, and entities to which the Listed Company assigns one of its activities'.<sup>768</sup> The law gives examples of these agencies, companies, etc. Although the provision can be applied during ongoing negotiations, it is vague and unclear. It does not contain details about the organisation of selective disclosure, in contrast to a parallel provision in the UK where selective disclosure is explained in detail with categories and examples.<sup>769</sup> Regardless of the lack of clarity about selective disclosure, it is a good development in the disclosure regime to ensure that inside

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<sup>764</sup> Brain McDonnel, above (n 699)17.

<sup>765</sup> Adel AlManea, above (n 9), 34

<sup>766</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 420. See also Mohammad Al-Mutairi, above, (n 24**Error! Bookmark not defined.**) 139

<sup>767</sup> CMA Executive Bylaws , Module Ten, Chapter Three Article 3-1-2

<sup>768</sup> *ibid.*

<sup>769</sup> DTR 2.5.7 'DTR 2.2 Disclosure of inside Information - FCA Handbook'.

information is protected and there is no leak. Forbidding third parties from disclosing material information is sufficient to achieve effective regulation to prevent insider trading.

## **6. Rumours and news**

A stock market is a place where rumours and news items can positively or negatively affect the price of shares.<sup>770</sup> Disclosure is meant to ensure that a company's share value reflects the performance of the company rather than the effects of speculation or rumours.<sup>771</sup> Given the impact of social media, speculation and rumours can inflict grave damage on the market. Most probably, rumours and news begin to circulate when a listed company delays disclosure and there are leaks that end up in the news. In some cases competitors will deliberately start rumours.<sup>772</sup> Hence many jurisdictions have adopted policies to respond to rumours and news, although these vary somewhat. The FCA disclosure rules, for example, do not require listed companies to comment on rumours in all cases; they may choose to refuse to comment.<sup>773</sup>

Disclosure regulations in Kuwait do not endorse a 'no comment' policy. All rumours and news about a listed company that are likely to have an impact on the share price or investment decisions must be addressed and responded to.<sup>774</sup> A listed company must respond immediately by denying or confirming rumours; the company is not required to notify or consult with the CMA before making such an announcement. In the absence of guidance from the CMA on this matter, this could potentially lead to excessive disclosure which would harm the interests of companies, especially given today's online environment where sites become platforms for rumours and speculation which can easily spread without citing any sources. Participant No. 2 highlighted the lack of procedures or a legal framework to control and mitigate online rumours. It is crucial to enhance awareness and understanding of disclosure obligations and the ways in which a company is required to respond to rumours.

Participant No. 2 stated:

Disclosure as a written law is effective and sufficient. The actual application can prove its effectiveness or lack of it. The CMA needs to work to improve their

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<sup>770</sup> Hummam Alqussi above (n 685) 440.

<sup>771</sup> Luca Enriques and Sergio Gilotta (n 423) 514.

<sup>772</sup> Jelena Lepetić, 'Public Disclosure of inside Information' (2012) 60 *Anali Pravnog fakulteta u Beogradu* 188, 203.

<sup>773</sup> DTR 2.7 'DTR 2.7 Dealing with Rumours - FCA Handbook' <<https://www.handbook.fca.org.uk/handbook/DTR/2/7.html>> accessed 31 January 2020.

<sup>774</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4-4

tools and mechanisms to enforce or apply disclosure regulations. A practical example would be that until now the CMA is unable to keep up with world developments, in addition to its inability to control the news on the social media. Although there is some referral from the CMA to the prosecutor regarding fake news, the efforts are not enough to control the markets. All these referrals are dismissed by the court because there are no clear procedures to control such rumours on social media.

Requiring listed companies to respond to all rumours is inconsistent with the risk-based approach to supervision. A company should pick a strategy to protect its interests and allocate its resources accordingly when it comes to commenting on significant rumours or news items. The CMA should allow listed companies to determine for themselves whether to comment or to adopt a 'no comment' policy. This obligation existed before the 2010 CML,<sup>775</sup> and it seems that the regulator's rationale was a belief in the importance of responding to the market; because Kuwait has a small stock market with only 175 listed companies, imposing an 'obligation to respond' to rumours and news was thought to protect both the market and investors.<sup>776</sup> Since Kuwait has only seven newspapers, it was deemed justifiable to insist on something more than a 'no comment' policy.

There is another argument to support the current CMA requirement for listed companies to issue a clarification regarding news and rumours, and this is the impact of culture on stock markets. The most modern news providers, such as Twitter and Facebook are platform for fake news and rumours and there is only general rule to regulate those platforms. There is no specific rules to organise those modern news provider in terms of the person responsibility to spread or post fake news and rumours. The person or organisation who initially posts the rumour on social media should be under legal responsibility and provide the CMA with clear rules to question them and punish them as well. The interviews data also confirmed this gap in the CML and its Executive Bylaws for not providing specific rules and regulations for modern news providers. Kuwait is a small society, and most investors make their investment decisions based on personal connections rather than analyses of financial statements.<sup>777</sup> It is necessary to provide rule to regulate news and rumours in modern news providers and establish the legal responsibility of the person or organisation who posts or spread fake news or rumours. Thus the CMA strategy to obligate the listed company to clarify the new news is justified given the

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<sup>775</sup> Adel AlManea (n 9Error! Bookmark not defined.). 25.

<sup>776</sup> Fahad Al-Zumai (n 70) 316.

<sup>777</sup> Khalid Saad Hulmi, *The Legal Structure of Stock Markets Exchange: Comparative Study Kuwait and Egypt* (Kuwait University Academic Publication Council 2010) 156. See also Hummam Alqussi (n 685) 449.

size of the Kuwaiti market and the effect that rumours may have upon it but in terms of the modern news providers, Kuwait must issue new rules to organise those platforms. In the long run, however, the CMA should seek to transform the Kuwaiti stock market by encouraging analysis and disclosure as the primary means for making investment decisions. The CMA can indirectly affect the market culture by improving market transparency and regulating the modern news providers.

However, this research argues that if the CMA wants to develop the market, it should consider trusting a listed company's judgement. The CMA should step away from the market and leave some self-regulation to listed companies. The main idea behind the risk-based approach is that companies are best situated to determine how to allocate their resources and define risk. Consequently, it is the companies' duty and responsibility either to comment on rumours or to choose to say nothing. The CMA should intervene only if a listed company inflicts damage upon the market.

## **7. Unusual trading activity**

One of the main purposes of the disclosure regime is to ensure that the value of a company's shares represents its past and future performance. One stock exchange philosophy considers that the performance of a company should be reflected in the price of its securities in the market.<sup>778</sup> Any unusual trading activity raises doubts about companies' performance. Regulations in Kuwait monitor unusual trading activity to protect the market.<sup>779</sup>

If an unusual trading activity occurs, Boursa and the CMA must warn the listed company and take the following steps.<sup>780</sup>

1. If a listed company decides that the unusual trading activity is due to material information previously disclosed through the appropriate procedure, it is necessary to re-disclose this information together with any changes in the previously disclosed material information.
2. If the unusual trading activity is due to speculation, news, rumors or other information, the listed company must immediately issue a comment.
3. If the unusual trading activity is due to leaked material information not previously disclosed by the listed company or where such disclosure has been delayed in accordance with Article (4-3) in this Module, the listed company must

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<sup>778</sup> Bernard Black, 'The Core Institutions That Support Strong Securities Markets' (n 12) 1567.

<sup>779</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4-5.

<sup>780</sup> *ibid*, Module Ten, Chapter Four, Article 4-5-1.



immediately disclose this information regardless of whether such disclosure is in the interest of the listed company or not.

4. If the listed company is not able to identify the reason behind the unusual trading activity, it must issue a general announcement indicating that there have been no recent developments likely to impact the Listed Company or its affairs in the way that would warrant such unusual trading activity.

In all cases, the CMA and Boursa have the authority to halt trading of listed company shares temporarily and take measures prescribed by the CML. Its provisions are stringent and do not allow for market self-regulation. The regulator's relationship with the industry is not based on a principle of trust, and companies must comply with regulations. The CML imposes a heavy burden by requiring a listed company to halt trading in its shares temporarily and explain its trading activity.

From the risk-based perspective, the regulator must determine the potential risks of unusual trading activities and makes its decision based on this assessment. A listed company must also assess the risks of unusual trading activity to protect its own interests. Requiring a listed company to take measures on the basis of its own assessment to protect its interest by taking sufficient procedures to identify and explain the unusual trading activity in stock markets. There is no need to impose additional rules on listed companies. This practice allows self-regulation and improves the quality of disclosure. Some academic commentators highlight that there is much unhelpful disclosure in stock markets because the CMA imposes a very strict disclosure obligation.<sup>781</sup> Developing the disclosure regime by adopting a risk-based approach will improve the type and quality of disclosure in stock markets. But regardless of this argument, the CMA strategy to oblige listed companies to clarify unusual trading activity aims to protect the investor from insider trading and market manipulation. This is a positive step to enhance investors' trust in Kuwaiti stock markets. The interviewees explained the importance of the clarification of unusual trading activity.

Participant No. 1 stated:

It is good development to obligate the listed companies to clarify unusual trading activity.

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<sup>781</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 585,564. See also Jamal AlOthman, above (n 544) 508.

Participant No. 2 said:

Unusual trading in stock markets is initial alerts of financial crisis, so the obligation of listed companies to clarify the trading activity is vital to provide adequate protection to investors.

Participant No. 3 said:

There is no doubt that the Kuwait stock market is in need of this obligation to clarify unusual trading activities. Otherwise big companies and family listed companies will manipulate the market.

Participant No. 4:

Announcing unusual trading is in fact a legislative necessity, to guarantee transparency and protection of the market from inside trading or manipulation.

Participant No. 5 said:

There is no harm to the market to request clarification from listed companies on unusual trading. It surely increases the market's transparency and integrity.

Participant No. 6 stated:

Disclosing unusual trading is an important tool that the CMA and Boursa must use to protect the markets, otherwise the key players in the stock markets manipulate the investors. The regulation of unusual trading has been more developed and up to date since the issuance of amendments in 2015. In fact, prior to the 2015 amendments the listed companies announced almost daily that there was no reason behind their unusual trading, which flooded the market with unnecessary announcements that confused investors and drove their attention away from important announcements. Now the listed companies do not need to justify the company's shares seeing unusual trading in stock markets until the CMA requests a clarification. In some cases, this provision might be misused by listed companies to avoid liability, as the CMA or Boursa do not request any justification to the trading although there is unusual trading.

## **8. Corporate insider watch list**

Academic commentators have criticised the disclosure regime in Kuwait for not having an insider list for market participants to identify individuals with access to inside information.<sup>782</sup> The amendments to the Executive Bylaws in 2015 introduced an insider list to provide adequate supervision of the disclosure regime. In the researcher's view, one of the positive changes in the new regulations is that disclosure now requires listed companies to name insiders.

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<sup>782</sup> Hummam Alqussi (n 685) 446. See also Adel AlManea (n 9) 26. and Abdualah Alshebli (n 4) 159.

The CMA requires a listed company to provide details about its insiders and submit a list of names to the CMA and Boursa.<sup>783</sup> An insider is a person who has access to inside information in the company. The identification of insiders in companies helps to prevent leaks and insider trading. It allows the CMA to focus on discovering insider trading in a given company by concentrating on a limited list of individuals who might have access to inside information. Additionally, it gives the listed company an opportunity to improve its internal monitoring to identify potential insiders and assess the risk each poses to the company. In the long term, this helps to develop and improve the company's management.

The insider list includes members of the board of directors and the executive body of a listed company and its subsidiaries. It also contains information about the parent company's access to inside information, either directly or indirectly.<sup>784</sup> Furthermore, the 2015 Executive Bylaws go beyond the list of visible insiders to include any other person or entity that is directly linked to the company and potentially holds inside information related to the listed company or its clients.<sup>785</sup> It also covers third parties who might have inside information about the listed company without confidentiality obligations.<sup>786</sup>

The listed company should take the necessary steps to ensure that other insider entities maintain a list of staff with access to inside information.<sup>787</sup> The listed company is required to update its insider list regularly, and any changes must be reported to the CMA and Boursa within five working days.<sup>788</sup>

It seems that the CMA disclosure rules for insider lists were transplanted from the FCA Disclosure and Transparency Rules (DTRs), which require the issuer to prepare such a list.<sup>789</sup> The only difference is that in the UK the listed company must prepare the insider list and submit it upon FCA request,<sup>790</sup> whereas in Kuwait a company is required to submit the insider list to the CMA and Boursa within a given timeline.<sup>791</sup> This, it is submitted, is a positive practice

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<sup>783</sup> CMA Executive Bylaws, Module Ten, Chapter Three, Article 3.5.

<sup>784</sup> *ibid*, Article 3.1.2-1.

<sup>785</sup> *ibid*, Module Ten, Chapter Three, Article 3.1.2-2. – 3-5.

<sup>786</sup> *ibid*, Article 3.1.2

<sup>787</sup> *ibid*, Article 3.5.1

<sup>788</sup> *ibid*, Article 3.5.1-2

<sup>789</sup> DTR 2.8 << <https://www.handbook.fca.org.uk/handbook/DTR/2/8.html?date=2016-03-07>>> accessed 31 January 2020.

<sup>790</sup> DTR 2.8.2A << <https://www.handbook.fca.org.uk/handbook/DTR/2/8.html?date=2016-03-07>>> accessed 31 January 2020.

<sup>791</sup> CMA Executive Bylaws, Module Ten, Chapter Three, Article 3.5.1-2.

because there are only 175 listed companies in the Kuwaiti stock market, so the practice of requesting an insider list according to a timeline is manageable.

The FCA provides more details and clarification regarding the insider list to help listed companies and issuers to apply the DTRs correctly.<sup>792</sup> Although the insider list rules have been transplanted from the UK regime, they can still be deemed a positive development in the Kuwaiti disclosure regime. The legal culture in Kuwait is increasingly aware of the importance of the insider list, and the discussion at the aforementioned CMA workshop<sup>793</sup> shows there is adequate understanding of its importance.

## **9. Form of disclosure**

Not all disclosures of information mean that the information is publicly available. Artificial or ineffective disclosure does not result in publicly available information – as, for example, when information is disclosed to a non-specialised publication that investors do not read. There are different requirements and procedures for making information public in an appropriate manner. Some jurisdictions impose specific requirements for publication methods, for example by requiring the transmission of information to a designated news agency; others only require releasing information to wide-ranging publications.<sup>794</sup>

The disclosure of material information increases the risk of litigation against firms if the disclosure is misleading or incomplete. For this reason, listed companies often reduce the amount of information provided to market participants to avoid litigation.<sup>795</sup> Also, a listed company may limit disclosure to a minimum to avoid breach of disclosure obligations while simultaneously failing to provide useful information to investors. Academic commentators have critiqued this form of disclosure, arguing that it does not supply enough information about the current performance of a company or the impact of an event.<sup>796</sup>

In Kuwait, the CMA has a disclosure form that listed companies must use to disclose material information.<sup>797</sup> Academic commentators had previously criticised the disclosure regime for

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<sup>792</sup> FSA, 'Markets Division: Newsletter on Market Conduct Issues' <[http://www.fsa.gov.uk/pubs/newsletters/mw\\_newsletter12.pdf](http://www.fsa.gov.uk/pubs/newsletters/mw_newsletter12.pdf)> accessed 18 March 2020.

<sup>793</sup> The CMA's workshop (n 719)

<sup>794</sup> IOSCO, 'Insider Trading How Jurisdiction Regulate It' [2003] IOSCO <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>> accessed 18 March 2020.

<sup>795</sup> Luca Enriques and Sergio Gilotta (n 423) 531.

<sup>796</sup> Abdullah AlHayyan and Moahamad AlMutari, above, (n 68) 400.

<sup>797</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4-6-1.

lacking such a form,<sup>798</sup> and the amendments to the 2015 Executive Bylaws were a response to this criticism. Currently, a listed company must use the CMA form to disclose material information to the CMA and Boursa.<sup>799</sup> Listed companies are compelled to have a website and post disclosed information, under threat of penalty.<sup>800</sup> During the CMA workshop (see above),<sup>801</sup> the Disclosure Department stated that presently it is not imposing penalties if listed companies do not have a website, but added that this might soon change. At the time of writing this thesis, the CMA has not imposed penalties on companies which do not post disclosed information. This is yet another example of unclear CMA policy that can shift abruptly.

A central message regarding disclosure obligations is to deliver enough good information about the listed company to enable market participants to make investment decision. The content of announcements is important to enhance trust and confidence in stock markets and ensure that investors have equal access to inside information, so eventually preventing insider trading.<sup>802</sup>

To complete the disclosure procedure, regulations require listed companies to submit two copies of a disclosure, one to the CMA and the other to Boursa. A fine is imposed when a company does not comply with this obligation. Filing a disclosure can be costly, as it requires intensive use of a company's resources,<sup>803</sup> and many companies do not have the capacity or ability to fulfil this obligation. Furthermore, the old-school practice of companies submitting disclosure forms either manually or by PDF did not serve the CMA's objective of raising local market standards to an international level. Additionally, in the past there were no standards to verify disclosed information: each department at the CMA exercised its judgement when assessing data. This method is costly and does not result in a coherent disclosure regime.

So a new method was launched in November 2015, when the CMA joined XBRL International to create a system that allows listed companies and other licensed companies to submit their disclosure forms using XBRL language.<sup>804</sup> The move was meant to improve the disclosure process by linking the disclosures to the CMA and Boursa (see Figure 2: The Disclosure

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<sup>798</sup> Abdullah Alshebli (n 4**Error! Bookmark not defined.**) 166.

<sup>799</sup> CMA Executive Bylaws, Module Ten, Chapter Four, Article 4-6-1.

<sup>800</sup> *ibid.*, Article 4-7.

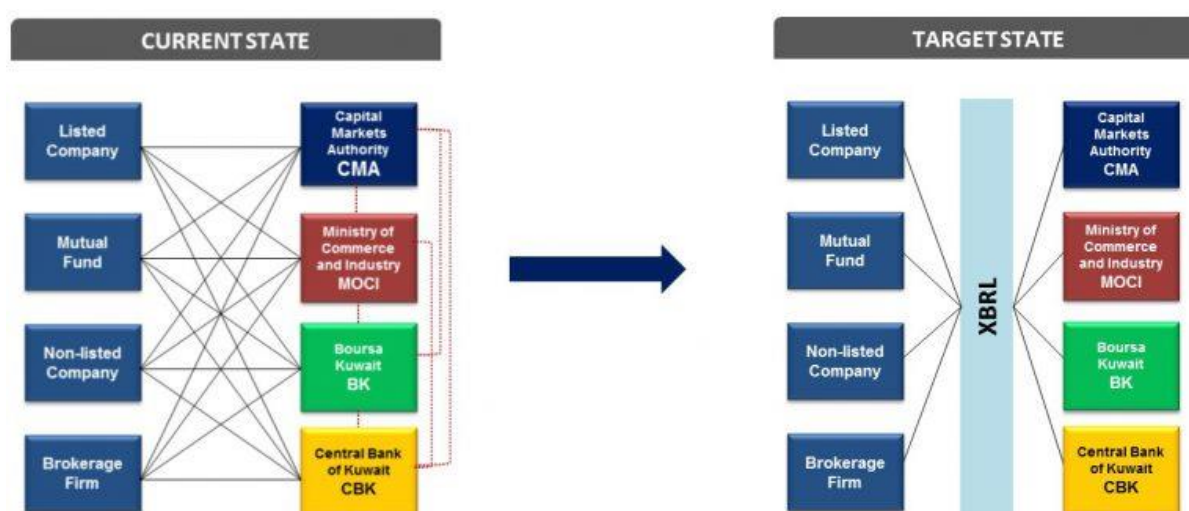
<sup>801</sup> The CMA's workshop (n 719)

<sup>802</sup> Brian McDonnell, above (n 699) 13.

<sup>803</sup> AlHayyan and Moahamad AlMuatari, above, (n 68) 404.

<sup>804</sup> Capital Markets Authority, 'Capital Market Authority Announces Membership of XBRL International' <<https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/369164>> accessed 18 March 2020.

procedures in Kuwait before and after using the XBRL system), and thereby reducing the company burden. Figure 2 shows the inconsistent methods that the CMA and Boursa currently use to collect the information: an insufficient and incoherent structure. In contrast, in the new method the XBRL framework validates the disclosed information and immediately informs the CMA and the submitting company about any shortcomings in the information. The submitted financial data will be promptly available to investors and other concerned persons. Further information, such as an insiders watch list, can be submitted and updated easily through XBRL.



Source: CMA Annual Report 2018/2019.

Unfortunately, at the time of writing this project has not been fully implemented in Kuwait capital markets because of a lack of cooperation between the CMA and other supervisory authorities.<sup>805</sup> An experiment in 2017 allowed listed companies to submit their disclosures through the XBRL framework voluntarily, but this failed due to technological challenges and the companies' lack of technical knowledge.<sup>806</sup> The CMA organised a workshop in May 2017 to explain the system and process for disclosing information using XBRL.<sup>807</sup> But although this is a significant development in the disclosure process, it had been only partially enforced by February 2019.<sup>808</sup> Hence there are still no links between the CMA and Boursa in terms of

<sup>805</sup> State Audit Bureau report for financial year 2017/2018 available at <<<https://www.sab.gov.kw/sabweb/>>> accessed 3 February 2020.

<sup>806</sup> The CMA, 'Electronic Disclosure System XBRL' (24 May 2017) available <<<https://www.cma.gov.kw/en/web/cma/awarenessevents/-/cmageneric/476117>>> accessed 18 March 2020.

<sup>807</sup> Capital Markets Authority, 'Electronic Disclosure System Using XBRL Language' <<https://www.cma.gov.kw/ar/web/cma/awarenessevents/-/cmageneric/476117>> accessed 3 February 2020.

<sup>808</sup> The CMA, 'The Capital Markets Authority Launches the Electronic Disclosure System XBRL as of today' (10 February 2019) available <<<https://www.cma.gov.kw/ar/web/cma/cma-board-releases/-/cmaboardreleases/detail/646131>>> accessed 18 March 2020.

submitted disclosures. A listed company is required to submit a disclosure to the CMA through XBRL and another disclosure to Boursa using procedures imposed by Boursa in 2018. There are no links between the CMA and the other supervisory authorities, Boursa and the CBK, which was the main purpose of creating the XBRL system in the first place. The old-school approach to disclosure is still employed, and it is necessary to upgrade current disclosure practice.

## **10. Conclusion**

The move towards risk-based supervision without a proper understanding of the expected changes is challenging, as it may require full-fledged reorganisation of the current regulatory framework and may also involve acquiring new sets of skills. This analysis showed that the CMA does not provide adequate information to apply the risk-based approach. There are no published policies or public statements about the adopted practices or regulations.

This chapter examines the obligation of listed companies to disclose material information to tackle insider trading. After highlighting the drawbacks of adopting an unclear definition of material information and links with the ‘prudent investor’ test, it proceeds along two lines. First, it argues that some provisions have been transplanted from the UK without taking into consideration cultural differences within the industry. Second, it questions whether the adoption of a risk-based approach is sufficient for defining material information in the stock market.

The chapter discusses developments in the Kuwaiti disclosure regime following the amendments to the Executive Bylaws in 2015. It is argued that these amendments overcome many of the previous regulatory challenges. The chapter introduces the legal framework for the disclosure of material information by determining the responsibility for disclosing it, as well as the timing of disclosure. The analyses show that Kuwaiti listed companies do not disclose proper information and do not justify their disclosure. Furthermore, the Executive Bylaws regulate selective disclosure and rumours and news items in the stock market. Although the CMA has not, as yet, introduced best practices to deal with rumours, especially online, it has taken into consideration the impact of the Kuwait local market culture. It has also proposed solutions for dealing with unusual trading activity in the stock markets and the obligations that a listed company must follow.

One of the critical developments in Kuwaiti disclosure regulations is the insider list, which the Executive Bylaws introduced to limit the impact and scope of trading using inside information. There is a significant relationship between legal developments and the use of market integrity to tackle insider trading and protect market participants. In this respect, CMA standards and policies are still lacking clarity. It is suggested that the CMA should adopt clearer policies to foster understanding with the industry and work towards applying a risk-based approach.



## Chapter 7: The Mechanics and Regulation of Insider Trading

### 1. Introduction

Insider trading is a sophisticated crime.<sup>809</sup> It needs proper regulation to protect market integrity and enhance investors' confidence and trust in the stock market. Insider trading threatens the financial regulator's objective of protecting the markets.<sup>810</sup> There are always new methods to conduct insider trading, which makes this is a complex crime.<sup>811</sup> Preventing illicit behaviours in stock markets is not an easy task, as these are moving targets. It is very common to find that only a small proportion of cases of insider trading result in convictions.<sup>812</sup>

Insider trading has been found in Kuwaiti stock markets, but the regulation is weak for many reasons. For example, insider trading was regulated before the CML was passed in 2010 but the law was not enforced,<sup>813</sup> and even after the CML the regulation is still weak. However, cases involving insider trading are rare.<sup>814</sup> Although the CMA refers reports to the prosecutor to investigate insider trading, most referrals have been dismissed due lack of evidence or insufficient grounds:<sup>815</sup> the only judgment issued in 2014 was against the chairman of Al Ahli Bank, who was fined approximately 1.5 million dinars (around £3,777.72) in the first instance court, although the appeal court reduced the fine to 100,000 Kuwaiti dinars (around £251,343).<sup>816</sup> Nonetheless, all the interviewees confirmed that there is insider trading in Kuwaiti stock markets, hence it is important to investigate the insider trading regulations to highlight the weaknesses in Kuwait's financial system.

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<sup>809</sup> Andrew Baker, 'Insider dealing' 141 in Nicholas Ryder, *Financial Crime in the 21<sup>st</sup> Century: Law and Police* (Edward Elgar, 2011) 141.

<sup>810</sup> Margaret Cole, 'Insider Dealing in the City' (2007) vol.4, issue 1 *Law and Financial Market Review*, 307, 307.

<sup>811</sup> Andrew Baker, above, (n 809) 141.

<sup>812</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700) 10

<sup>813</sup> Fahad AlZumai. above (n 70) 229. See also Abdullallah AlHayyan and Moahamad AlMuatari, above, (n 68) 50.

<sup>814</sup> Fatima AlShuraian above, (n 4) 7.

<sup>815</sup> The CMA Report for the Financial Year 2018/2019 (in Arabic)

<sup>816</sup> Kuwait Appeal Court, Case No. 15/2014, 17/2013, 214/2013 issued on 25 November 2014. Page 12

It is essential to design an efficient framework to tackle insider trading in order to have strong securities markets,<sup>817</sup> and the law must consider both legal and cultural aspects of the crime. A risk-based approach helps to achieve this target by requiring firms to manage the risk associated with insider trading rather than simply complying with a set of rules issued by a financial regulator. The approach consists of three core steps to establish effective regulation: first, understand the insider trading framework and risks; second, set rules to mitigate these risks; and third, enhance cooperation between supervisory authorities to prevent insider trading.

This chapter explains insider trading as an illegal action, and how a regulator should control it to protect the market and its participants. It focuses on the criminal regime, as the CML has no civil regime to tackle insider dealing, unlike the UK approach. The research investigates the CML and its Executive Bylaws to regulate insider trading in stock markets.

### 1.1 Brief background to insider trading

It is useful to understand the history of insider trading regulation, moving it from being a non-criminal to a criminal act.

Relevant regulation has taken some time and gone through several phases to reach an agreement to criminalise insider trading.<sup>818</sup> There were controversial debates between scholars about whether or not to regulate the practice,<sup>819</sup> and there is a significant volume of academic material on each side.

One side is against regulating insider trading because it facilitates movement of shares before inside information is disclosed. These scholars base their arguments on the grounds that the opportunity to exploit inside information may come ‘once every ten years for each listed company’,<sup>820</sup> hence there is no need to regulate insider trading. They support their argument with accurate pricing theory, in which shares should reflect a company’s performance and the current information on the market only. Full

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<sup>817</sup> Bernard Black, ‘The Core Institutions That Support Strong Securities Markets’ above (n 12**Error! Bookmark not defined.**) 1583.

<sup>818</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 6.

<sup>819</sup> In UK, the insider dealing became criminal offence on 23 June 1980 when the Companies Act 1980 came into force. Margaret Cole above (n 810) 308.

<sup>820</sup> Harry McVea, ‘What’s Wrong with Insider Dealing’ (1995) vol.15. issue.3 Legal Studies, 390, 400.

disclosure does not achieve its ultimate goal, but only helps short-term traders and speculators to gain profit or avoid loss.<sup>821</sup> They support their argument based on the idea that it is fair compensation for a company employee to benefit from inside information, and claim that insider trading is a victimless crime.<sup>822</sup> It does not have individual victims, and regulations should protect the people's interest. They go further, arguing that insider trading benefits the markets by improving market accuracy and efficiency, because information is moved into markets more quickly.<sup>823</sup>

These scholars introduce public choice theory as a basis against regulating insider trading. Investors engage in the stock market because they believe they know something that others do not, based on either data analysis, personal connections or inside information, so it is their choice to participate in the market. In addition, insider trading does not affect either allocative efficiency or the cost of capital, because, as Cox states, 'any change that affects the cost of capital for all firms at the same rate will not affect the relative comparisons made by investors'. He refutes the claim that insider dealing drives investors from the stock market into other investments. His argument is set within the context of shareholders' preferences for investments.<sup>824</sup>

This argument ultimately fails for three main reasons.<sup>825</sup> First, it is uncertain that insider trading would benefit the stock markets by improving market accuracy and efficiency. Investors will bear a higher level of risk because of uncertainty over the market's reaction to this valuable information. Secondly, in terms of transaction costs, investors do not receive compensation for extra transactions. Thirdly, this practice does not give equal access to information and investment; in other words, a change that affects the cost of capital will not benefit the markets and investors, as Cox claims.

The opposing side supports arguments for regulating insider trading because of its impacts on the stock market. There are many principles and theories which advocate regulation of insider trading and consider it a criminal offence. In developed capitalist countries, insider trading is regulated because it harms maintenance of a fair and orderly

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<sup>821</sup> Henry Manne, *Insider Trading and the Stock Exchange* (Free Press 1966) 455.

<sup>822</sup> Harry McVea, above, (n 820) 403.

<sup>823</sup> Macey page 7-12, see also Harry McVea, above, (n 820) 404.

<sup>824</sup> James Cox cited in Harry McVea, above, (n 820) 397.

<sup>825</sup> Harry McVea, above, (n 820) 397-400. See Henry Manne above (n 821) 459.

market.<sup>826</sup> The most effective argument is that it is unfair practice to use inside information without providing the same opportunity to other investors.<sup>827</sup> Share prices must reflect all published and available information, so the price represents the company's performance and helps an investor to make an informed decision.<sup>828</sup> There is no fairness when a person uses inside information to gain profit or avoid loss and other investors have no idea about this information. It is unethical to use the privilege of inside information to serve self-interest.<sup>829</sup>

Furthermore, there are many reasons to regulate insider trading, mostly related to economic arguments, such as the damage that the insider causes to investors and markets, and the use of material information as a property right.<sup>830</sup> Beyond economics, there is a significant literature on a rational basis for prohibiting insider trading related to its effect of impairing allocative efficiency in the stock markets.<sup>831</sup> It is immoral and unethical behaviour for an insider to take advantage of information available to him/her by virtue of his/her position in a company when this information is not revealed to other investors.<sup>832</sup> There are substantive arguments to support regulating insider trading, thus most developed countries, such as the US and the UK, do so.<sup>833</sup>

Regardless of the academic debate on whether or not regulate insider trading, in most countries it is illegal. International organisations recommend principles and standards to reform financial regulation and prevent insider trading. The IOSCO objectives and principles of regulation are designed to establish strong securities markets.<sup>834</sup>

In Kuwait, before the 2008 financial crisis the regulator viewed insider trading as a criminal offence, but the laws were unclear and insufficient.<sup>835</sup> After the crisis the legislature reformed the regulations to ensure that insider trading transactions are

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<sup>826</sup> Harry McVea, above, (n 820) 412-413.

<sup>827</sup> Craig W. Davis, *Misappropriations, Tippees and the Intent-to-Benefit Rule: What we can Still Learn from Casy, Roberts* (Seton Hall Law Review, 2004) 270-271.

<sup>828</sup> Harry McVea, above, (n 820) 393.

<sup>829</sup> Gary Lawson, 'Ethic of Insider Trading' (1988) 11 Harvard Journal of Law Public Policy, 727, 733.

<sup>830</sup> Stephen Bainbridge, 'The Law and Economics of Insider Trading: A Comprehensive Primer' (2001) Available at SSRN 261277, 398.

<sup>831</sup> Harry McVea, above, (n 820) 412. See also Margaret Cole, above, (n 810) 307-308.

<sup>832</sup> Margaret Cole, above, (n 810) 308.

<sup>833</sup> Philip Summe, Kimberly McCoy, 'Insider Trading Regulation: A Developing State's [respective]' 6 4 Journal of Financial Crime, 311, 311.

<sup>834</sup> IOSCO, available at <<https://www.iosco.org/search/>> accessed 18 March 2020.

<sup>835</sup> Ahmed Al-Melhem, above (n 9) 78 Fahad AlZumai. above (n 70) 503.

prohibited. As the research interviews show, this regulation is a positive improvement to enhance investor protection in stock markets. The CML explicitly regulates insider trading in Articles 118 and 119, and the 2015 amendments to the CML Executive Bylaws introduced further details. There is no independent law to regulate insider trading in Kuwait: it is part of the CML. The 'Market conduct' module sets out details of insider trading and its transactions,<sup>836</sup> and forms the legal basis for regulating these practices in Kuwaiti stock markets. Finally, if the CML and its Executive Bylaws do not cover certain factors regarding criminal liabilities of insiders, the CMA should apply Kuwait Criminal Law No. 6 of 1960 (KCL).

It was a positive development in the Kuwaiti legal system to recognise insider trading. All interviewees confirmed this as being a great improvement in the financial sector.

Participant No. 1 stated:

Since the issuance of CML, there is huge development to tackle insider trading. For example, now it is officially forbidden for insiders to talk about inside information in private gathering with friends and family.

Participant No. 2 explained:

The latest amendments (in 2015) added the third type of insider, which is 'others'. This is a very positive development.

Participant No. 3 stated:

It was clear and obvious that the CML needed to regulate inside trading and protect the markets.

Participant No. 4:

The parliament finally woke up and issued a law to regulate insider trading.

Participant No. 5:

As experts, we were in position to see how the law was weak to tackle insider trading. The CML had a huge impact on the markets: at least it sets ground rules to forbid such trading.

Participant No. 6:

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<sup>836</sup> The Executive Bylaws, Module Fourteen.

There is positive development in the CML, especially in the area where there are two ways to trade in stock markets. One of them is through an online company like KMEFIC, a 'registered company to trade in stock markets'. Another is through having a registered number from Boursa and trading directly. In the online trading, through a company, the real investor is unknown to Boursa but online company knows the investor. Previously, Boursa could not know the real investor through the online company, but now with the new amendments, Boursa can know who is trading through the online company. It is a great development.

Participant No. 7:

Article 118 of the CML gives the judge and prosecutor the legal basis to prosecute insiders and protect the markets.

In the UK insider trading is regulated by the Criminal Justice Act 1993 (CJA) and the FSMA 2000, so the UK uses both criminal and civil regimes to combat the problem. The civil regime does not exist in the Kuwait system. A number of amendments were made to the FSMA 2000 following the implementation of the EU Market Abuse Directive and Financial Services Act 2012, to reflect the new policy of the civil regime. Even the CJA was subject to a major revision by the virtue of the Market Abuse Directive, which sets a minimum standard across EU markets. Furthermore, the Code on Market Conduct and the DTRs, which clarify and explain the general statutory prohibition of the civil regime and organise disclosure obligations, were also remodelled after huge amendments to the original FSMA 2000. Most amendments to the FSMA were made in 2005, 2011, 2014 and 2016. In the 2005 amendment, seven categories of abusive behaviour were introduced. In 2011 FSMA s. 118 and 118A was amended to adopt a broader definition of market abuse. In 2014 several sections of the FSMA were changed to bring the law into line with the Market Abuse Directive. The 2016 amendment introduced alterations to the FCA's powers to investigate and detect abusive behaviour.<sup>837</sup>

## 1.2 Criminal versus administrative/civil regimes

This research focuses on the criminal regime in evaluating financial regulation under the CML, as Kuwait does not recognise a civil regime to regulate insider dealing. This shortcoming was highlighted by the interviewees, who confirmed that Kuwait needs a

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<sup>837</sup> Ester Herlin-Karnell and Nicholas Ryder, *Market Manipulation and Insider Trading* (HART 2019) 81.

civil regime in this area (Participants Nos 2, 3 and 4). There are major differences between administrative/civil and criminal regimes regarding insider trading. In a criminal regime there is lower percentage of convictions<sup>838</sup> because it requires a high standard of proof, which is difficult to obtain in a sophisticated offence like insider trading.<sup>839</sup> It takes a knowledgeable prosecutor who is able to understand the crime and convict the perpetrator. The administrative/civil regime requires lower standards of proof to convict insider trading, and focuses more on the whole ambit of activities that lead to an offence.<sup>840</sup> Such a regime aims to provide a comprehensive framework to supervise financial transactions in stock markets,<sup>841</sup> and give the financial regulator flexibility to enforce the law and apply sufficient deterrent in the market to reduce financial crime. Importantly, an administrative/civil regime applies not only to natural individuals but also to juristic persons which might commit insider trading offences; in most jurisdictions a criminal regime applies to individuals only.<sup>842</sup> A criminal regime can impose fines and imprisonment for up to five years for insider trading offences, while a civil regime can only enforce administrative penalties.

There are no court procedures in an administrative regime; it only includes disciplinary board procedures at the financial regulator to impose penalties. In a criminal regime there is a court process which requires the insider to appoint a lawyer to defend him/her. Hence the criminal regime is more costly than the administrative/civil regime for both parties. A significant difference between criminal and administrative/civil regimes is that the latter does not require proof of the insider's intention to commit the crime.<sup>843</sup>

Administrative enforcement gives the financial regulator adequate tools and powers to prevent and punish market misconduct. It provides unlimited financial sanction, public censure and other administrative penalties, as the UK approach shows.<sup>844</sup> Overall, the administrative regime does not replace the criminal regime in the financial sector, but

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<sup>838</sup> Andrew Baker, above, (n 809) 159.

<sup>839</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 5.

<sup>840</sup> Andrew Baker, above, (n 809) 159.

<sup>841</sup> *ibid.* 158.

<sup>842</sup> *ibid.* 159.

<sup>843</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 160.

<sup>844</sup> Karen Harrison and Nicholas Ryder *The law Relating to Financial Crime in the United Kingdom* (2016) 2nd ed Routledge)156.

<sup>844</sup> As discussed in Enforcement chapter.

helps to ensure full disclosure of any material information that might be used to commit insider trading. Sanction of any incomplete, fake or delayed disclosure by administrative penalties decreases the use of inside information. Both regimes work together to provide effective regulation against insider trading. The criminal regime has a more deterrent approach than the administrative regime:<sup>845</sup> it threatens perpetrators with imprisonment, which leads traders to think twice before committing an insider trading offence.

The experts interviewed confirmed that the administrative regime is important to protect investors. They explained that a criminal regime provides more deterrence than an administrative regime, and the CMA must work harder to reform the administrative regime to increase its penalties for illegal activities. The interviewees felt the criminal regime is a positive development in the CML. They confirm how anti-insider trading regulation has developed since the issue of the CML, but also feel there are shortcomings in the financial regulations to prevent and punish insider trading in terms of the civil regime.

Participant No. 2:

The criminal and disciplinary regulations are completing each other to punish and deter the violating company. Each system has gaps that allow lawyers and violators to avoid the punishment. Having both systems helps the application of the law and ensures punishing the violators.

Participant No. 3:

The current criminal regime to regulate insider dealing is excellent, especially after adding the 'others' as a type of insiders.

Participant No. 4:

The CML regulation on insider trading is fine, but there is no recognition of the civil regime in Kuwait system. Another important point to highlight that the law does not clarify its purpose. Let's say, the purpose of the law is to protect the investor then the civil regime to claim for compensation must be organised in the CMA Law. Currently, there is no recognition of the civil regime in CMA Law at all. This is a huge deficiency and must be amended immediately. Identification of insider trading risk

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<sup>845</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 505.



The first step in the risk-based approach is to identify insider trading risks. The regulations must be clear and sound in terms of a legal basis of responsibilities to punish insiders in stock markets. The regulator must set out a variety of ways to identify insider risks.<sup>846</sup> To this end, the CMA obliges listed companies to adopt a sound system of risk management and internal audit.<sup>847</sup> Listed companies should be able to identify risks and set proper procedures to deal with them.<sup>848</sup> An independent risk management unit must identify, measure and monitor risks associated with the company's activities on a periodic basis.<sup>849</sup> The risk identification system must be developed and amended when necessary to be able to recognise uncommon risks. In addition, the CMA obliges listed companies to have internal audits to review the company's activities in terms of soundness, data accuracy and operational effectiveness.<sup>850</sup> An independent audit firm shall be assigned by a listed company to evaluate the internal audit system and prepare a report.<sup>851</sup> A report must be submitted to the CMA every year. Another auditing firm must be assigned every three years to evaluate the internal audit unit.<sup>852</sup> All these rules ensure that listed companies have proper procedures to identify and assess internal risk and are able to take the necessary precautions to mitigate these risks. The reports help the CMA to evaluate the controls in place in a listed company and judge the effectiveness of the internal oversight functions, the history of the company's compliance with regulation, and the history of suspicious transactions and monitoring reports. This is in line with IOSCO Principles to establish an internal function to manage risk.<sup>853</sup> The question is whether these units and firms will be able to identify insider trading risks in stock markets within the current regulatory framework.

### 1.3 Framework and definition

Insider trading can be defined as 'the unfair use of material, non-public information concerning an issue of securities [which] threatens to undermine the integrity of the

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<sup>846</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> Accessed 18 March 2020.

<sup>847</sup> The Executive Bylaws, Module 15, Chapter 6, Article 6-1

<sup>848</sup> *ibid.*

<sup>849</sup> *ibid.* Article 6-3

<sup>850</sup> *ibid.* Article 6-6

<sup>851</sup> *ibid.* Article 6-9

<sup>852</sup> *ibid.*, Article 6-9

<sup>853</sup> Principle 31 Of IOSCO Objectives and Principles

national securities markets'.<sup>854</sup> It means a person takes advantage of non-public information available by virtue of his/her position in a company to achieve his/her own interest, when such information affects the share price of the company (either positively or negatively).<sup>855</sup> This practice damages the stock market's integrity and reputation, as it results in unequal access to information and ultimately leads investors to abandon the market.<sup>856</sup> The first thing people check before investing in stocks is the financial regulator's ability to provide effective protection to the market and its participants,<sup>857</sup> and the first objective of the IOSCO Principles is 'the protection of investors' – and one of the major areas is protecting investors from insider trading.<sup>858</sup> Rules must be designed to achieve these regulatory objectives, so anti-insider trading regulation should be efficient and sound.

The first obvious deficiency in Kuwait's regime is the lack of a framework to regulate insider trading. There is no clear definition of the offence, and no exact framework for insider trading in the CML and its Executive Bylaws. It seems that implementation of the anti-insider trading regulation is based on scholars' interpretations of the rules. As the interviews reveal, there is a lack of understanding of insider trading as a crime, and industry employees share valuable information about their work at private gatherings in Kuwait without understanding the consequences. Since the issue of the CML in 2010 there has been no serious effort by the CMA to raise public awareness about insider trading and its effect on market integrity.

In contrast, the UK legislation defines insider trading in the CJA and provides a substantive explanation to cover four areas: insiders,<sup>859</sup> inside sources,<sup>860</sup> inside information<sup>861</sup> and types of insider activities.<sup>862</sup> It gives a clear framework to regulate insider trading, which is defined as 'trading in organised securities markets by persons

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<sup>854</sup> Oliver Colvin 'A Dynamic Definition of and Prohibition Against Insider Trading' (1991) 31 Santa Clara Law Review, 603, 633.

<sup>855</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 2.

<sup>856</sup> Abdullah AlHayyan and Moahamad AlMutari, above, (n 68) 609.

<sup>857</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 4.

<sup>858</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > accessed 18 March 2020.

<sup>859</sup> The CJA 1993, Section 57-1

<sup>860</sup> Ibid, Section 56.

<sup>861</sup> Ibid. Section 52.

<sup>862</sup> Ibid. Section 52.

in possession of material non-public information and has been recognised as a widespread problem that is extremely difficult to eradicate'.<sup>863</sup>

It is important for Kuwait's legal system to introduce a clear and sufficient framework for insider trading, because the regulations in the CML must be followed and enforced as written by the legislator.<sup>864</sup> A rule-based approach to regulations must follow the letter of the law, not its spirit. CMA decisions cannot go beyond the law as laid down in the CML and its Executive Bylaws. This is command-and control-regulation, which is a strategy whereby policymakers set targets and standards to be achieved by regulated firms, and subsequent penalties will apply if those targets and standards are not met.<sup>865</sup> Kuwait applies a rule-based approach as a general principle in regulating insider trading, but this is clearly not effective. It is currently inflexible in adopting new tools and powers to capture new insider trading methods.

It is advisable that the CMA adopts a risk-based approach to set out a framework for its priorities in supervising markets and tackling insider trading. The anti-insider trading regime must be supported by guidance and examples to ensure a good understanding of the unique methods used in the crime.<sup>866</sup> The difficulty of establishing sound regulation is that it must be well drafted to criminalise insider activities.<sup>867</sup> It must be well designed, and deliver coherent protection to the market and its participants.

#### 1.4 Definition of inside information

It is important to set a clear definition of inside information to establish responsibility for the crime.<sup>868</sup> If the definition is unclear or lax, the insider will not be punished for the crime and the stock markets will struggle to prevent insider trading. There is no unified definition of what constitutes inside information in the global financial sector:

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<sup>863</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n700) 31.

<sup>864</sup> Abdullallah AlHayyan and Moahamad AlMuatari, above, (n 68)611.

<sup>865</sup> Neil Gunningham and Peter Grabosky, *Smart Regulation* Oxford Clarendon Press (1998) 39

<sup>866</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 3 February 2020.

<sup>867</sup> Ana Carvajal and Jennifer Elliott, above, (n 424)

<sup>868</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020.

each jurisdiction has its own definition.<sup>869</sup> There are, however, some commonalities. Undoubtedly, the task of defining what constitutes inside information in practice is challenging, but such definitions are indispensable.

This research argues that the CML and its Executive Bylaws fail to provide a clear and comprehensive definition of inside information. The interviews confirm this, and companies still struggle to understand the difference between material information and inside information. In general, inside information can be defined as unpublished information that affects the company's value in the stock market.<sup>870</sup> The unpublished information must influence a person to buy or sell shares. According to the UK approach, the CJA identifies four elements that define inside information.<sup>871</sup> The first is that the information must not be available in the public realm; that is, it must be confidential. Secondly, it must be related to a fact or an event. Third, there must be a relationship between the information and its source. Whether information is considered inside information or not depends on its direct or indirect relationship with the issuers of financial instruments. The fourth and final element is that the information must be sensitive or significant enough to have an impact on the value of shares.<sup>872</sup> The FSMA lists another four elements to determine inside information. First, it should be related to a qualifying investment traded on specified markets, whether directly or indirectly.<sup>873</sup> Qualifying investments can be described as 'all investment of a kind which is admitted to trading under the rules of any prescribed market'.<sup>874</sup> This is different to the CJA, which relates information to a particular security or issuer. Secondly, the information should be precise. Thirdly, the information should not be generally available. Finally, the information will have a significant effect if it is made public. It seems that the FSMA adopts a broad definition of inside information to ensure that all illegal activities can be captured and punished by civil penalties.

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<sup>869</sup> Emiliós E Avgouleas, *The Mechanics and Regulation of Market Abuse: A Legal and Economic Analysis*, above, (n 469)

<sup>870</sup> Nicholas Ryder, *Financial Crime in the 21<sup>st</sup> Century: Law and Police* (Edward Elgar, 2011)

<sup>871</sup> The CJA1993, section 56.

<sup>872</sup> Jelena Lepetić, above, (n 772) 188, 193. 193. See also Gilbert Manning Warren, 'The Regulation Of Insider Trading In The European Community' (1991) 48 Washington and Lee Law Review 1037, 1059.

<sup>873</sup> s118C FSMA

<sup>874</sup> Raghda Al-Qatanani, above (n 260) 133. See also FSMA 2000 (Prescribed Markets and Qualifying Investments) Order 2001 s. 5 << <http://www.legislation.gov.uk/ukxi/2001/996/made>>> accessed 18 March 2020.

The IOSCO Principles note two elements that must be present if information is to be considered inside information: confidentiality and materiality.<sup>875</sup> Based on these elements, this research analyses the definition of inside information in Kuwait's legal system. Each element of the definition of inside information must be clear and sound to produce effective anti-insider trading regulation. The key practical implication is the confusion between inside information and material information in Kuwait,<sup>876</sup> and there is no guidance to clarify this for companies. Before the 2015 amendments to the CML and its Executive Bylaws, academic commentators argued that there was no legal definition of inside information, which put market integrity at risk.<sup>877</sup> Furthermore, CML Article 119 included news items as inside information. This provision was criticised, because using news for insider trading cannot be a basis for a criminal case.<sup>878</sup> This was addressed in the 2015 amendments, and 'news' was deleted as inside information.

The CML has undergone a series of updates to attract investors to the Kuwait stock market.<sup>879</sup> One of the goals was to facilitate the detection of insider trading by providing a clear definition of inside information, and Article 1 of the bylaws defines it as: 'Information or data not disclosed to the public, which if disclosed would affect the price or trading of securities.'<sup>880</sup> There are many shortcomings in this definition. It does not determine whether the information is accurate and correct, potentially mixing it with rumours and speculation.<sup>881</sup> For example, if a person has knowledge of a specific market rumour, this can be treated as having inside information. It makes the scenario worse if the rumour (which is price-sensitive information) is incorrect. The lack of certainty in this definition is probably the most significant and worrying aspect for the financial sector. A rule-based approach limits regulation to the stated provisions in the law, which will affect the application of a risk-based approach to regulate insider trading. It is

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<sup>875</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 7 February 2020.

<sup>876</sup> Samer Abdullallah, above, (n 688) 50.

<sup>877</sup> Adel AlManea, above (n 9**Error! Bookmark not defined.**) 23., see also Abdullah Alshebli, above, (n 4).

<sup>878</sup> Adel AlManea, 'above, (n 9) 18.

<sup>879</sup> AlHayyan and Moahamad AlMuatari, above, (n 68)60.

<sup>880</sup> The Executive Bylaws, Module 1.

<sup>881</sup> Abdullallah AlHayyan and Moahamad AlMuatari, above, (n 68) 92.

essential to ensure that the inside information is correct, to establish an insider's liability for the trading.

This definition consists of two elements: confidentiality and influential impact. Inside information must be material information. Materiality is defined with reference to the importance of the information, its scope and its source.<sup>882</sup> Materiality is the most important factor in the definition of inside information.

#### 1.4.1 Importance

Most jurisdictions consider information material when it becomes public and significantly affects the price of securities. For instance, UK regulations state that such information 'is "price-sensitive information" in relation to securities, if and only if the information would, if made public, be likely to have a significant effect on the price of the securities'.<sup>883</sup> Some jurisdictions take a further step to increase precision. The materiality of information might be evaluated according to its potential impact on the behaviour of market participants or by reference to its sensitivity, i.e. its effect on prices in the stock market.<sup>884</sup> Other jurisdictions, like Malaysia, catalogue the events that contribute to the definition of material information.<sup>885</sup>

For information to be considered inside information it must not be publicly available. Accordingly, there may not be publicly available data linked to the information, such as an annual report. In short, the information may not be in the public domain. As the CMA has not published any guidelines about inside information, this has led to debates about how the public domain is defined, which proves the lack of clarity of the regulation. According to academic commentators, when information has been shared with a few people (even if they are outsiders) it is not considered to be in the public domain.<sup>886</sup> If a group of individuals who do not work in the listed company possess confidential information, the information is located outside the public domain. The researcher

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<sup>882</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 28 January 2020.

<sup>883</sup> The CJA 1993. Article 56

<sup>884</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020.

<sup>885</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020.

<sup>886</sup> Ahmed Almulhem, above, (n 9) 60, see also Adel AlManea, above (n 9)18.

disagrees with this assumption. The information must be disclosed through procedures to be officially in the public domain, otherwise it is crime to discuss or disclosure this information. This is especially so because investors in Kuwait make investment decisions based primarily on personal connections.<sup>887</sup> Considering the stock market size and the culture, it is necessary to evaluate the impact of a rule redefining confidentiality and the public domain to ensure that no one outside a company has knowledge of inside information, otherwise there may be legal consequences.

Another suggestion is to modify the phrase ‘information inaccessible to the public’.<sup>888</sup> The FCA definition of inside information in CJA 1993 Article 56 and FCA Handbook section 2.2.1 refer to the definition in Article 7 of the Market Access Directive. Both definitions are clear and sound, and provide an explanation of inside information.<sup>889</sup> It is the researcher’s view that this increases the precision of the rule far better than the comparable CMA provision. It clarifies that once information is disclosed to ‘a few people’, it may no longer be considered confidential. It directly addresses the risk inherent in defining inside information in terms that are more effective and enforceable.

Another factor to consider is whether a price movement in the stock market is sufficient to consider inside information material. The CMA definition includes the effect of the information on the price and trading of securities. There is no specification of how to determine influence, and no theoretical percentage movement in price that might guide the listed company in determining the influence of information on price. It remains primarily a subjective determination on the part of a company, which relies on a hypothetical reaction by prudent investors with knowledge of the information. The adoption of a more precise definition of inside information is recommended, including a more exact determination of the level of influence of given information on the market price as a percentage movement.

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<sup>887</sup> Abdualлах AlHayyan and Moahamad AlMuatari, above, (n 68) 58.

<sup>888</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 28 January 2020

<sup>889</sup> The CJA 1993, article 7, see DTR 2.2.1 Disclosure Guidance and Transparency Rule, FCA Handbook’ available <<https://www.handbook.fca.org.uk/handbook/DTR/2/2.html>> accessed 18 March 2020, Market Abuse Regulation, Article 7

#### 1.4.2 Scope

Most jurisdictions classify ‘material inside information’ as information that is related to the issuer, the markets and other factors, such as whether or not trading using the inside information influences the liquidity of the traded security. None of this link to the issuer exists in Kuwait. The CML Executive Bylaws give 29 examples of the scope of potential material information,<sup>890</sup> and thematically outline what may be considered as material information. Participant No. 5 stated that it is CMA policy to stick to these examples as a framework to supervise the disclosure of material information. This rule-based approach with set examples does not help the CMA to tackle insider trading, since the crime is a moving target and there are many types and ways to conduct it. Hence this provision is insufficient for the CMA to prevent insider trading in stock markets.

#### 1.4.3 Sources of information

This approach focuses on persons who deal with sensitive information and those connected with the issuer to determine whether information is material. For example, a person who is using inside information must be aware that the source of the information is an insider. The purpose of this condition is to determine the scope of the inside information. In practice, however, this makes enforcement difficult. The 2015 amendments to the CML introduced a new provision requiring the creation of an ‘insider list’ that must include all individuals with access to inside information. Its rationale was to tackle insider trading by identifying primary and secondary insiders; previously, Kuwaiti regulators had linked the materiality of information to its first source only.<sup>891</sup> This is a positive development in regulation, but the third type of insider, the ‘other’, is not determined. The vagueness of the insider list is further proof of the lack of clarity of the regulation in defining inside information.

Beyond this, the interviews confirmed that the CML and its Executive Bylaws do not provide a clear definition of inside information, and listed companies are confused between the two concepts of material information and inside information.

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<sup>890</sup> The Executive Bylaws, Module Ten, Article 4-1-1.

<sup>891</sup> Samer Abdullah, above, (n 688) 60.



Participant No. 3 insisted:

It seems that the current definition is unclear to define inside information and material information, which confuses companies to disclose the right information and there is no advisory firm to listed companies in this regard. The CMA must amend and reform the current regulation to clarify the definitions and bridge any gaps.

Participant No. 4 stated:

The definition of inside information is not as accurate as it should be. Sometime inside information is not important to be disclosed or in other cases the information has already been disclosed. The accurate definition is supposed to be 'material non-public information'. Kuwait has a rule-based regulation; therefore, the definition of inside information must be accurate and precise. In French, the regulations define the information as privileged information. The US defines the information as material non-public information and the UK approach defines it as insider information, which again confirms that Kuwait translated the English law.

Participant No. 5 explained that the CMA follows a strategy regarding the disclosure of material information by listed companies whereby if they do not disclose it, it will be considered as inside information:

The markets need time to understand inside information and it is necessary to increase awareness about the material information to be disclosed in the stock markets. In fact, the Executive Bylaws explain the material information in detail and provide examples about material information as well to ensure that listed companies disclose the right information. The CMA refers listed companies to the Disciplinary Board for any violation in disclosure regulation or delay in disclosing material information. There is a custom in the CMA that punishes any company that violates examples provided in the bylaws about material information and any other scenarios not covered by the examples. The CMA usually send a warning letter to alert the company about the violation. The CMA adopts a flexible policy because the listed companies need time to understand the mechanism of disclosure in stock markets.

It is unacceptable that, after almost ten years of implementation of CML and its Executive Bylaws, the CMA still sticks to the provided examples. There are more types of material information that needs to be disclosed immediately to avoid insider trading than just the examples cited. Undisclosed material information becomes inside information that an insider can use to gain profit or avoid loss. The lack of a clear definition of inside information in the CMA leads listed companies to disclose

unimportant information when fulfilling their disclosure obligations. These unimportant disclosures do not achieve the goal of giving investors equal access to the companies' valuable information.

## 2. Insiders

A clear definition of insiders is necessary to identify an insider trading risk, to supervise insiders who may potentially commit the crime and to enforce the law against criminal insiders. Each jurisdiction has its own policy to determine an insider, whether the definition is broad or narrow;<sup>892</sup> the definition depends on the regulator's objectives and the purpose of the law. In general there are two types of insiders in stock markets: primary and secondary.<sup>893</sup> The question is whether or not Kuwait's definition of insiders achieves its purpose.

Kuwait's definition went through two phases. Prior to the 2015 amendments to the Executive Bylaws there was a very narrow definition of an insider<sup>894</sup> covering people who are in a position to obtain inside information as decision-makers – in other words, primary insiders. The law did not recognise other types of secondary insiders, such as a tippee who knows or should be aware that the information is from an original source (primary insider) and trades based on this information, or a sub-tippee who discovers inside information in unusual circumstances (an accidental insider) and trades based on this information.<sup>895</sup> The CMA and the courts could not add secondary insiders because they must follow the written law. Primary or permanent insiders obtain inside information by virtue of their position in a company, whether as director, worker or shareholder of an issuer.<sup>896</sup> In most cases primary insiders have a fiduciary duty or contractual relationship with the company.<sup>897</sup> The definition also covered temporary insiders: professionals not employed by the company but who provide services to the

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<sup>892</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 15 January 2019 28 January 2020. 7

<sup>893</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 35.

<sup>894</sup> Previous article 118 of the CML, Adel AlManea, above, (n 9) 77, Samer Abdullallah, above, (n 688) 118.

<sup>895</sup> Mohammad Al-Mutairi, above, (n 24**Error! Bookmark not defined.**) 95-98.

<sup>896</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 12. See also Andrew Baker, above (n 809) 158

<sup>897</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020.

company and have access to inside information,<sup>898</sup> such as accountants, lawyers and advisers. Academic commentators criticised the insider definition because it did not cover secondary insiders and others, unlike the UK approach,<sup>899</sup> and did not provide sufficient definition to protect the markets.

The second phase came after the 2015 amendments to the Executive Bylaws. The current Kuwait definition of an insider is ‘any person, in view of his position, has access to information or data of material effect on a Listed Company that is not available to the public’.<sup>900</sup> The 2015 amendments expand the definition of the insider in CML Article 118 to include primary, secondary and others. The bylaws state:

A Person is considered an Insider in a Listed Company in the following cases: 1. Members of the Board of Directors and members of the executive body of a Listed Company, its Subsidiary Companies and a Parent Company who have access to Inside Information related, directly or indirectly, to a Listed Company or its clients. 2. Any other Person or entity who is directly linked to the company and holds Inside Information related to the Listed Company or its clients including, but not limited to, the Parent Company, the Auditor, banking firms, advisory firms, Credit Rating Agencies, information technology companies, and entities to which the Listed Company assigns one of its activities.<sup>901</sup>

This wide definition covers people who are in a position to obtain inside information or might reach inside information, and others who might obtain information accidentally.<sup>902</sup> The directors of the company are not the only persons who possess inside information; the notion of an insider encompasses all those who, by virtue of their position or their business or professional relationship with the company, should be considered as a primary insider.<sup>903</sup> A secondary insider is a person who obtains inside information either directly or indirectly (accidentally<sup>904</sup>) from a primary insider in the knowledge that it is

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<sup>898</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 13 March 2020. 8

<sup>899</sup> Adel AlManea, above, (n 9) 29. See also Samer Abdullah, above, (n 688) 118.

<sup>900</sup> Executive Bylaw Module One, Chapter One, See also Bursa Kuwait Rulebook (April 2019) available at <<https://www.boursakuwait.com.kw/regulations/rules-and-bulletins/rulebook>> accessed 14 February 2020.

<sup>901</sup> Executive Bylaws, Module Ten, Chapter Three, Article 3-1-2

<sup>902</sup> Ahmed Al-Melhem, above, (n 23) 80. See also Adel AlManea, above (n 9), 22. Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 715.

<sup>903</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 5. See also Andrew Baker, above (n 809) 158

<sup>904</sup> Accidental insider is a person that neither has access to inside information, nor was tipped by a person who has access to such information but learned inside information due to special circumstances. The

unpublished price-sensitive information and that it is an offence to deal or trade based on that information.<sup>905</sup> This can include someone who has inside information based on illegal activities,<sup>906</sup> such as hacking. There are important points to highlight in this insider definition.

First, the definition only recognises natural persons who engage in insider trading and does not criminalise juristic persons who might commit the crime to achieve a company's interest by encouraging another person to sell or buy shares based on inside information.<sup>907</sup> Participants Nos 1, 3, 4 and 5 highlighted the failure to recognise a juristic person as an insider as a shortcoming in the law (see below). A Kuwait Appeal Court judgment on 25 November 2014 stated that a local bank benefited from insider trading in stock markets by approximately 1.5 million Kuwaiti dinars (£3,777.72) but the bank was not fined because the law only recognises natural persons.<sup>908</sup> Clearly, this judgment proves there is insufficient regulation to prevent insider trading. Kuwait must reform the CML to adopt a civil regime for regulating insider trading, and include juristic persons as a type of insider to be punished for any criminal transaction. This issue has been highlighted in many conferences and by academic commentators, but the CMA has not suggested any amendment to the law.<sup>909</sup> This raises the question of whether the CMA really wants to implement effective regulation to prevent insider trading. However, the UK approach also only recognises natural persons as able to perpetrate insider trading offences, according to the CJA.<sup>910</sup> It refers to 'individuals' who commit the crime, which means it does not consider a company as an entity able to commit insider trading. The UK approach overcomes this shortcoming by enabling

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IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 15 January 2019 28 January 2020. 9

<sup>905</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 15 January 2019 28 January 2020. See also Andrew Baker, above (n 809) 158

<sup>906</sup> Abdullāh AlHayyan and Moahamad AlMuatari, above, (n 68) 715.

<sup>907</sup> It's worth to mention the France Criminal Law recognize legal person like company to commit insider trading.

<sup>908</sup> Kuwait Appeal Court, Case No. 15/2014, 17/2013, 214/2013 issued on 25 November 2014. Page 12

<sup>909</sup> Khalida Saad Hulmi, above, (n 777) 901. See also Ahmed AlMulham, above (n 9 **Error! Bookmark not defined.**) 45. Abdullāh AlHayyan and Moahamad AlMuatari, above, (n 68) 58. Samer Abdullāh, above, (n 688) 33.

<sup>910</sup> Section 52 of the CJA 1993. See also Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 34.

the civil regime to tackle insider trading to include juristic persons.<sup>911</sup> This indicates that Kuwaiti financial regulation has been transplanted from the UK CJA provisions without understanding the purpose of the law. It is suggested that juristic persons should be considered as insiders as well as natural persons.

Participant No. 1 highlighted:

The CMA followed the UK CJA approach of not recognising the juristic person as an insider. It is the time to change this strategy and adopt a wider definition to include a juristic person who gets benefits from insider dealing.

Participant No. 3:

I highlighted this point on many occasions before the issuance of the 2015 amendments, including conferences. Companies must be considered as a type of insider to protect market integrity and investors, but it seems that serving the listed companies' interest is more important than protecting the markets.

Participant No. 4:

The current law only recognises persons, but companies do insider dealing crimes as well when they benefit from the trading. It is necessary to extend the law to cover the company as a legal person.

Participant No. 5:

Obviously, the CML in 2010 adopted a narrative approach to regulate insider trading because the markets were not ready to implement all new regulations, and the 2015 amendments did not consider companies as insiders. After implementing the CML for ten years it is the right time to consider including a juristic person as an insider.

Secondly, the 2015 amendments failed to provide a clear determination of a third type of insider beyond primary and secondary: the 'others', which is anyone in possession of inside information.<sup>912</sup> Expanding the definition of insiders to include 'others' has occurred only in books, with no application of the stated provision. Furthermore, the Executive Bylaws require listed companies to provide details of insiders to the CMA and Boursa, which then scrutinise this list of insiders on a regular basis to ensure there is no unusual trading. In case of the 'others' type of insider, how can the CMA and

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<sup>911</sup> The MAR, article 8, section 5.

<sup>912</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 715.

Boursa observe their trading? The CML provides no guidance to identify this type of insider, and there was disagreement among the expert interviewees as to whether including ‘others’ as insiders is a positive or negative development. Participants Nos 4, 5, 6 and 7 see it as a provision that is impossible to enforce, while Participants Nos 1, 2 and 3 see it as a positive development for the CML to adopt a wide and broad definition of insiders.

Furthermore, an important issue in the Kuwaiti definition is whether to consider MPs as insiders. Scholars criticise their omission,<sup>913</sup> because MPs draft and issue laws and regulations and obtain inside information by virtue of their position in the National Assembly.<sup>914</sup> Although it is important to specify MPs clearly in the regulations, the ‘other’ type of insider added in the 2015 amendment to the definition includes MPs.

The interviewees had different views regarding the ‘other’ type of insider. Four felt that including this third type without providing elements to identify such insiders will eventually result in a provision that is hard or impossible to implement.

Participant No. 5 stated:

Post-2015 amendments, the insider definition became wider to include ‘others’ as a type of insider in insider dealing crimes. As far as I know, there is no referral from the CMA to the prosecutor in which the insider was an ‘other’ as per the latest amendments to the law. In fact, the CMA observes insider trading in the stock markets because companies provide a list of insider names to the CMA and Boursa, but the ‘others’ cannot be included on the list. Therefore, there is no clear way for the CMA to observe the ‘others’ trading in stock markets.

Participant No. 4 said:

There are different types of insiders and the Kuwaiti law does not distinguish between them. That led scholars and judges to interpret the law. The current interpretation does not serve the purpose of the law. In my opinion, the hacker has been criminalised indirectly by the CMA through its bylaws. The article stated that ‘everyone who has obtained the information illegally’. This means that the hacker is a type of insider who obtained the information unlawfully. Of course, this provision is vague and needs further clarification to punish a hacker as an insider. The regulation

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<sup>913</sup> *ibid.* 405

<sup>914</sup> National Assembly is the legislature branch which responsible to draft and issue the law in the Kuwait.

should be clear and precise to serve its purpose, but the current provision is vague and can't be applied in court.

Participant No. 7 stated:

Although I have not reviewed a case where the accused person was the third type of insider as the 2015 amendments added, I found it very difficult to convict a person who is not included in the list of insiders. As you know, if there is a doubt the judge will always rule in favour of the accused person.

Participant No. 6 added:

The 2015 amendments received a wider application to tackle insider dealing by adding 'other' as a type of insider. Practically speaking, it is difficult to tackle or capture 'other' in insider dealing because Kuwait is a very small society/country and there is no investigation team like SEC who would investigate the crime like policemen would do. So even with the 2015 development, there is no difference in terms of the application of law.

The other three interviewees look at it from a different perspective: all developed countries consider the third type of insider, and Kuwait must do the same.

Participant No. 1 stated:

There is a difference between the regulation of the law and its application. The regulation must cover all possible situations to provide a comprehensive structure to regulate insider trading. Including a third party as an insider is necessary to have a solid and effective law and regulation like the developed countries.

Participant No. 3 highlighted:

Including 'other' as a type of insider is a good and important development. All the developed countries have added three types of insider including the term 'others'. Although having different types of insiders did not achieve the regulator's deterrence objectives, it is good development in stock markets.

Thirdly, the distinction between primary and secondary insiders is important in terms of imposed sanctions and enforcement procedures. Some jurisdictions impose harsher sanctions on primary insiders than on secondary.<sup>915</sup> Kuwait does not differentiate

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<sup>915</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCPD145.pdf>>> accessed 18 March 2020. 7

between primary and secondary insiders in terms of the amount of sanction.<sup>916</sup> To provide sufficient deterrence, enforcement and sanctions must be appropriate: the punishment of someone in a decision-making position in a company must be different to that of any other employee in the company. Academic commentators argue that there is unfairness and injustice in the CML because there is no distinction in the punishment of insiders between issuer and receiver.<sup>917</sup> Criminal punishment does not deter insiders in either case because the punishments are insufficient. This indicates that the CML provides lax and inadequate regulation to punish insiders, and the interviews confirmed this.

Participant No. 4 stated:

The 2015 amendments were not sufficient, especially regarding Article 118 about insider dealing. The amendment extended the definition of the insider to include other by stating that ‘everyone who deals...’ This provision does not classify the insider types at all. For example, even the elevator man can be one of the ‘other’. Then the questions become the punishment. Should it be different for the issuance of the information and other? We can’t blame the CEO who leaks the information like the person who received the information accidentally (elevator man). The CEO’s punishment must be much more severe and more deterrent than the elevator man. In the US and the UK, the laws distinguished between the person who issued the information and the person who received the information. For example, if I worked for a listed company and provided information to my colleague to buy stock in the market and someone heard our conversation and did the same, the punishment should not be of the same severity for me and for the person who overheard us.

Fourthly, the Kuwaiti approach does not require the insider to receive personal benefits:<sup>918</sup> the benefits of the insider trading could be for others. It is positive practice not to limit the benefits to the insider only, but to include any member of the insider’s family or company. This broad approach helps to punish insiders on a wide scale.

On the other hand, the UK approach defines an insider as a person who possesses inside information and knows that it is inside information, and a person who possesses inside information and knows that it comes from an insider source.<sup>919</sup> The definition of insiders

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<sup>916</sup> CML, Article 118.

<sup>917</sup> Abdullah AlHayyan and Moahamad AlMuatari, above, (n 68) 93.

<sup>918</sup> CML, Article 118.

<sup>919</sup> the CJA 1993, Section 57.



in the UK is clear, and is found in CJA s. 57: ‘Insiders: (1) for the purposes of this part, a person has information as an insider if and only if: (a) it is, and he knows that it is, insider information; (b) he has it, and knows that he has it, from an inside source.’ It covers primary and secondary insiders, and introduces the tippee as a third party who receives inside information and use it for his/her benefit. It has a broad approach to establishing insider trading liability, and contains a policy statement to explain and clarify the law. It does not require inside information to be obtained legitimately, so even if individuals obtain the information illegitimately it will be considered as inside information and will be covered legally.<sup>920</sup> In both Kuwaiti and UK systems, insider trading liability is established when a person possesses inside information and knows the nature of this information even if they obtained it from illegal activities like hacking. This delivers a broad framework to regulate insider trading.

Finally, a risk-based approach to regulation must be built on a clear identification of insider trading risk, and the core basis of this concept is ‘who is the insider?’. An insufficient definition of insiders affects the supervision and enforcement process. It should be a priority of the financial regulator to be able to identify insiders who could potentially engage in insider trading.

### **3. Prohibited activities**

Insider trading regulation provides a framework to prevent insiders from engaging in certain activities in stock markets. It is important to identify the prohibited activities carefully: the definition must not be too narrow, which leave loopholes, or too broad, such that it impairs legitimate trading.<sup>921</sup> A balanced definition of prohibited activities takes into consideration the historical, cultural and economic context of each jurisdiction.

In the UK approach there are three main prohibited activities:<sup>922</sup> firstly, *dealing* in price-affected securities on the basis of inside information;<sup>923</sup> secondly, *encouraging* another

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<sup>920</sup> The Executive Bylaws, Module Fourteen, Chapter Two, Article 2.4

<sup>921</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 28 January 2020. 9-10

<sup>922</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 34.

<sup>923</sup> The CJA 1993, Section 52.

person to trade based on inside information;<sup>924</sup> and thirdly, *disclosing information* to another person.<sup>925</sup> To establish insider trading liability, a person should know that he/she possesses material non-public information from a primary source and acts in one of the prohibited ways with the intention to commit the offence. This means that the regulations do not extend to refraining from dealing: the accused must actually deal in the stock markets for it to constitute an insider trading crime.<sup>926</sup> With the encouragement offence, the insider must encourage another person to deal in stock markets for it to be considered an offence; regardless of whether or not the other person actually deals in the market, the liability arises if the insider encourages someone to believe or gives reasonable cause to believe that the insider has inside information relating to price-affected securities.<sup>927</sup>

In contrast, Kuwaiti regulations classify insider offences into four types of action:<sup>928</sup> the insider cannot *benefit* from inside information, cannot *take advantage* of such information, cannot *disclose* it and cannot *provide or give advice* based on inside information. It is important to note that an insider trading offence needs an actual action by the insider to constitute an offence.<sup>929</sup> The provisions use the terms ‘sold’, ‘purchased’, ‘disclosed’ and ‘gave’ to express insider action in engaging in insider trading: insider trading is a positive action and is not committed if a person does not take any action.<sup>930</sup> This means the law does not extend to recognising an abstention from dealing or attempted dealing in stock markets. Insider trading is a complex crime which needs more effective rules to establish insider liability, and should extend to include attempted dealing to provide comprehensive rules to criminalise insider trading.

The regulations consider insider trading to be a crime affecting the stock market regardless of whether any damage happens or not:<sup>931</sup> it is considered a crime and the insider should be punished even if there is no damage, because it is in the public interest

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<sup>924</sup> *ibid.*

<sup>925</sup> *ibid.*

<sup>926</sup> Andrew Baker, above (n 809) 155.

<sup>927</sup> *ibid.* 155.

<sup>928</sup> The CML, Article 118.

<sup>929</sup> Adel AlManea, above, (n 9) 45.

<sup>930</sup> *ibid.* 59.

<sup>931</sup> *ibid.* 46.

to have a strong market protected from insider trading.<sup>932</sup> It is a crime against the integrity of the stock market as a whole, and thus insiders should be punished based on conducting one of the prohibited actions.

Some key points must be highlighted in Kuwait's regulation. Prior to the 2015 amendments, academic commentators criticised the insider trading regime because it did not consider encouraging another person to trade based on using inside information to be a banned activity.<sup>933</sup> They also criticised the clarity of regulation, and there is no distinction between who benefited and took advantage of insider information, as discussed below.<sup>934</sup> Interestingly, many of these criticisms were addressed in the 2015 amendments.

In terms of the insider behaviour to commit the offence and there is no distinguish between benefited and took advantage of inside information in English language whereby in Arabic language makes huge difference. The first situation where the insider benefit from inside information, it means that there is profit from using this information either selling or buying shares. Where in the second situation took advantage, it means the insider maybe avoid loss money and the first situation cannot capture this act if it is not written in the second type of insider trading. A rule-based approach influences the regulation of insider trading by ensuring that all possible situations are addressed in the regulation.

In the UK approach it is prohibited to *deal* in securities whose price is affected by the inside information.<sup>935</sup> Insider trading is outlined in a broad definition of dealing that covers any acquisition or disposal of a security.<sup>936</sup> The UK courts and financial regulator can intervene to clarify the insider trading regulations, whereas in Kuwait's rule-based approach the court must follow the literal word of the law. Kuwaiti insider trading regulations are designed in a narrow way, and offences must be determined precisely in the regulations and explained in the law for an act to be considered as an offence.

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<sup>932</sup> The CML, Article 118 and 119.

<sup>933</sup> Ibid. 50. see also Humam Alqussi above (n 685) 127.

<sup>934</sup> Adel AlManea, 'above, (n 9Error! Bookmark not defined.) 55. Samer Abdullallah, above, (n 688) 120.

<sup>935</sup> CJA 1993, Section 52.

<sup>936</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700) 36.

After the 2015 amendments Kuwait adopted a wider approach to determining prohibited insider activities, but it did not ban encouraging another person to trade in the stock market using inside information.<sup>937</sup> This is unlike the UK approach, which considers encouraging another person to trade based on inside information to be an offence.<sup>938</sup> A reform of this type is needed to extend the CMA's power and enable it to capture insiders who encourage others to trade using inside information: this would address the difficulty in capturing insider trading based on family and personal connections.<sup>939</sup> From a cultural perspective, people are influenced in their investment decisions by their family connections, so outlawing encouragement to sell or buy shares reduces the influence of personal connections in the market. For example, the most famous insider trading in Kuwait stock markets happened in 2013, and the primary and secondary insiders were brothers.<sup>940</sup> Both were found guilty of using inside information to gain profits in stock markets.<sup>941</sup> It is clear that trading based on family/personal connection is common in Kuwait, thus it is necessary to reform the law to criminalise encouraging another person to trade based on inside information and to punish people who do not have an obvious relationship like brotherhood.

Kuwait regulation bans insiders from giving advice based on inside information. It was a positive step to include giving advice as a prohibited act, but academics criticised the fact that this prohibition initially only applied to primary insiders.<sup>942</sup> The amended law in CML Article 118 expands this application to include secondary insiders. In both Kuwait and the UK, insiders are not allowed to disclose inside information; this means that simple disclosure of inside information alone, without any further action, is banned. This ensures that insiders will be punished if they disclose any inside information.<sup>943</sup>

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<sup>937</sup> CML, Article 118.

<sup>938</sup> CJA 1993, Section 52.

<sup>939</sup> Humam Alqaussi, above, (n 685) 600 see also Ahmed Al-Melhem, above (n 9) 98-101.

<sup>940</sup> Kuwait Appeal Court, Case No. 15/2014, 17/2013, 214/2013 issued on 25 November 2014, unpublished judgment

<sup>941</sup> Sharq newspapers available at << <https://www.al-sharq.com/article/03/03/2014/-الأهلي-تغريم-رئيس-5-مليون-دينار> >> accessed 18 March 2020. see also Kuwait Appeal Court, Case No. 15/2014, 17/2013, 214/2013 issued on 25 November 2014, unpublished judgment

<sup>942</sup> Samer Abdullallah, above, (n 688) 120.

<sup>943</sup> Adel AlManea, 'above, (n 9) 60.

The 2015 amendments made it a prohibited act for insiders to ‘transfer or cause to be transferred Inside Information directly or indirectly to other people’.<sup>944</sup> This is disclosure of inside information in another sense, and there is no point in adding such a provision when the same article already says that insiders should not disclose inside information – it is obvious that disclosure includes transfer of inside information. However, the provision can be justified because of Kuwait’s rule-based approach: the legislators aim to cover every possible situation and interpretation of the law.

Furthermore, the offence is committed when an insider actually carries out one of the prohibited activities: this is the time of the offence.<sup>945</sup> Kuwait’s insider trading regulation only recognises the positive act of the insider, not any intention to act. In the UK an offence is committed if the insider has any prior negotiations or agreements to commit the offence.<sup>946</sup> The UK approach views agreeing to dispose of a security as dealing in securities, so the time of the offence is the time of the agreement, without any dealing actually taking place. This gives wider protection to market participants to ensure that insiders do not enter into any illegal agreement to commit insider trading. It is essential to highlight the time of the offence to provide sufficient evidence. The critical time the offence is committed should be the time of the agreement, regardless of whether the individual was acting as principal or agent.<sup>947</sup> The agent can rebut an insider trading accusation if he/she provides evidence that he/she acted as agent without knowledge of illegal action.<sup>948</sup> However, the time of the offence is important to establish criminal liability for insider trading. The positive action of the insider is essential to incur criminal responsibility in Kuwait, whereas in the UK agreeing to commit the offence is criminal.

This analysis shows how a rule-based approach influences the design of regulation. It obliges policymakers to imagine every possible scenario for insider trading, and regulate them all. It needs expertise to design rules that cover all possible situations, and the current insider trading regulation shows that this expertise is lacking in some areas. An insider must actually commit the act to establish liability and prove that he/she has

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<sup>944</sup> The Executive Bylaws, Module Ten, Chapter Three, Article 3-3-1

<sup>945</sup> Adel AlManea, ‘above, (n 9Error! Bookmark not defined.) 50.

<sup>946</sup> The CJA 1993 section 55 (2) (3)

<sup>947</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700)6.

<sup>948</sup> The CJA 1993 section 53.

the knowledge and intention to engage in insider trading: the insider must be in possession of inside information and undertake one of the prohibited activities.<sup>949</sup> The offence is a combination of actually doing the act and the intent to commit the crime: both elements must exist to establish insider liability under criminal law.

#### 3.1.1.1 Territorial scope of the offence

In establishing insider liability it is important to know where the activities happened. The globalisation and accessibility of stock markets gave the regulator concerns about the limitation scope of the law.<sup>950</sup> Trading venues have changed and markets have become global, allowing traders to deal in a wide variety of products and markets.<sup>951</sup> An investor can access any stock exchange in the world, so it is important for a regulator to set out its jurisdiction to ensure that insider trading regulation is effective.

Kuwait's CML does not address the territorial scope of insider trading, even in its Executive Bylaws; one has to look at the general criminal law, in the form of KCL No. 6 of 1960. The KCL is outdated and not suited to regulate a sophisticated crime like insider trading. However, according to KCL Article 11, any person who commits a crime in the territory of Kuwait and its affiliates shall be subject to Kuwait criminal law. Any person committing an insider trading transaction outside the territory of Kuwait cannot be subject to the KCL, but if insiders as initial actors or their accomplices commit an insider offence wholly or partly in the territory of Kuwait, they shall be subject to the KCL.<sup>952</sup>

There are a few key points in this article. First, it requires that the insider trading offence must take place fully or partly in Kuwait, meaning that some elements or factors of the committed offence should be within Kuwaiti jurisdiction.<sup>953</sup> The law does not provide effective regulation for insider trading: there is a shortcoming in the ability to capture such trading if the insider commits the crime outside Kuwait. For example, if a non-

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<sup>949</sup> Andrew Baker, above (n 809) 155.

<sup>950</sup> Adel AlManea, above, (n 9) 59.

<sup>951</sup> Janet Austin, 'Unusual Trade or Market Manipulation? How Market Abuse is Detected by Securities Regulators, Trading Venues and Self-Regulatory Organizations' (2015) 1 Financial Regulation Journal, 263, 264.

<sup>952</sup> There is no translation of the Kuwait Criminal Law. It stated article is a translation of the researcher.

<sup>953</sup> Ahmed Al-Melhem, above (n 9Error! Bookmark not defined.) 103.

Kuwaiti insider who has material unpublished information sends an order to sell or buy shares in Kuwait's stock market while he/she is outside Kuwait, the crime is committed wholly outside Kuwaiti jurisdiction and the KCL cannot capture or punish the perpetrator. The current KCL does not provide sufficient coverage of insider trading offences. It is suggested that the legislature should review the territorial scope of the CML and its Executive Bylaws to allow financial experts to regulate this complex topic and its unique characteristics.

Secondly, if the insider is a Kuwaiti national, KCL Article 12 stipulates that he/she will be subject to the KCL even if the whole crime is committed outside Kuwait. The rule is suitable for other crimes, but is insufficient to regulate insider trading because listed companies have a huge majority of directors and employees who are not Kuwaiti nationals. It is like a free ticket to commit insider trading offences: a person can obtain inside information by virtue of his/her position in a listed company, then commit the crime outside Kuwaiti jurisdiction where no rules apply to him/her. It is significantly important to amend the current law to add non-Kuwaiti insiders.

The UK approach regulates the territorial scope of insider trading, taking into consideration the complexity of the crime. The CJA 1993 outlined the territorial scope of insider trading offences, which can only be committed by a professional intermediary in the following circumstances:<sup>954</sup>

- he was within the UK at the time when he is alleged to have done any act constituting or forming part of the alleged dealing; or
- the regulated market on which the dealing is alleged to have occurred is one which, by an order made by the Treasury, is identified as being regulated in the UK; or
- the professional intermediary was within the UK at the time when he is alleged to have done anything by means of which the offence is alleged to have been committed.

An individual is not guilty of an offence falling within insider trading unless:<sup>955</sup>

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<sup>954</sup> The CJA 1993, section 62.

<sup>955</sup> The CJA 1993, section 62.

- he was within the UK at the time when he is alleged to have disclosed the information or encouraged the dealing; or
- the alleged recipient of the information or encouragement was within the UK at the time when he/she is alleged to have received the information or encouragement.

The UK statute aims narrowly at insider trading that takes place in the UK, and the statute does not apply if the essential element of the crime takes place outside UK jurisdiction.<sup>956</sup> It is the same as the Kuwaiti approach in terms of the essential element or whole crime being committed outside national jurisdiction, hence both systems are disorganised.

Another point confirming the narrow focus of insider trading rules in the UK is that the offence must take place in a regulated market.<sup>957</sup> This means that face-to-face trades between individuals are not precluded, probably leaving it up to individuals to ensure they have equality of information.<sup>958</sup> The only ‘off-market’ transactions under the regulation and enforcement of the CJA are when the person trading relies on a professional intermediary or is himself/herself acting as a professional intermediary.<sup>959</sup>

### 3.1.2 Intention

The criminal regime has harsh penalties in comparison with administrative sanctions, including imprisonment for up to five years and substantial fines.<sup>960</sup> Hence most countries require the prosecutor to provide evidence that the accused person intended to commit the offence.<sup>961</sup> The criminal regime for insider trading demands such evidence, which means proving that the perpetrator knows that he/she has inside information and trades in stock markets based on this information.

The question is whether Kuwait’s CML requires intention to establish insider liability. CML Articles 118 and 119 do not mention a special intention<sup>962</sup> to commit the offence,

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<sup>956</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above (n 700) 46.

<sup>957</sup> The CJA1993, section 52 (3).

<sup>958</sup> Andrew Baker, above (n 809) 156.

<sup>959</sup> The CJA 1993, section 52 (3).

<sup>960</sup> CML, Article 118.

<sup>961</sup> The IOSCO, ‘Insider Trading How Jurisdiction Regulate It’, (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 28 January 2020. 12

<sup>962</sup> Special intention is a set of conditions and requirements in the intention to consider the accused person is perpetrator.



which means the general provision of the KCL must apply in requiring proof of the accused person's intention to commit the crime.<sup>963</sup>

Furthermore, Articles 118 and 119 use phrases requiring the perpetrator's knowledge when committing an offence. It makes sense that the criminal regime requires higher standards of proof, because it relates to the freedom of individuals.<sup>964</sup> It cannot be effective and sufficient without ensuring that an accused person has the intention and will to commit the offence.<sup>965</sup> This is the main difference between the administrative and criminal regimes.

It is thus essential to ensure that an insider is aware that he/she possesses inside information and either directly or indirectly trades on a stock market based on this information.<sup>966</sup> The insider must be aware that the information is not public for it to be considered as insider trading. There is an important line between a trader with good intentions who believes that the information is public and an insider with bad intentions who knows that the information is not yet public.

The UK approach is similar to the Kuwaiti approach: the criminal offence of insider trading requires the prosecutor to prove that the accused person has the intention to commit the offence by knowing that he/she is using inside information, or the prosecutor has sufficient reason to believe that the accused person knows that this is inside information.<sup>967</sup> The UK approach overcomes the difficulty in proving a person's intention by enabling the civil regime to ignore intention when considering insider trading.<sup>968</sup> This civil regime helps to punish individuals and legal persons who commit insider trading in stock markets. It is advisable for the CMA to adopt a new civil regime to regulate insider trading in Kuwaiti markets.

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<sup>963</sup> The KCL Article 40

<sup>964</sup> Abdualah AlHayyan and Moahamad AlMuatari, above, (n 68) 67.

<sup>965</sup> Humam Alqaussi, above, (n 685) 23.

<sup>966</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at << <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 28 January 2020.

<sup>967</sup> The CJA 1993

<sup>968</sup> The FCA handbook, Market Abuse Regulation, 1.2.3 available << <https://www.handbook.fca.org.uk/handbook/MAR/1/2.html>>> accessed 14 February 2020.

#### 4. Mitigation of insider trading risk

A risk-based approach cannot succeed in mitigating risks if this is seen as the job of only one department.<sup>969</sup> Cooperation between departments and supervisory authorities is essential to have a proper risk-based approach and oversee companies adequately.<sup>970</sup> The CMA must establish a policy to allocate its resources to areas of higher risk of insider trading, based on information obtained from off-site or on-site visits or submitted reports. This means that the CMA must determine the frequency and intensity of periodic supervision based on the level of risk that a company poses to the CMA's objectives, and set its priorities accordingly. CMA staff must be trained to recognise the potential for insider trading and notice any unusual activities in the markets, but it seems there is no programme to train CMA staff in this area.

The main challenge faced by the financial regulator in tackling insider trading is how to detect and prove the offence. The interviews reveal that insider trading is a complex and infrequent crime, which means it is hard to supervise the markets. It is essential to prove the time of the offence to know whether or not an insider trading transaction has taken place. Determining the time of the criminal offence enables the authority to discover the insider's intention to commit the crime from his/her activities before and after the transaction.<sup>971</sup> For example, the disclosure obligations require the insider to disclose inside information, so if he/she did not disclose it, it should be considered as a breach of the disclosure obligations. This is the first lead to discover an insider's intention to commit insider trading.<sup>972</sup> The main issue is to determine the exact time of committing the illegal act to establish insider liability. The unclear rules in identifying the exact time of the offence affect the regulator's ability to prevent the crime.

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<sup>969</sup> Andrew Haynes, 'The Effective Articulation of Risk-Based Compliance in Banks' (2005) 6 *Journal of Banking Regulation*, 146, 149-150.

<sup>970</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 3 February 2020.

<sup>971</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700)171. Adel AlManea, 'above, (n 9Error! Bookmark not defined.) 50.

<sup>972</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020. 3

The researcher asked the experts about ‘the CMA’s efforts to tackle insider trading in the stock markets’. The difficulty in detecting insider trading was highlighted by all interviewees.

Participant No. 1:

There is a difficulty in proving the insider trading in practice, especially if the trader is a friend of the insider. How could the CMA prove this kind of risk?

Participant No. 2:

It is extremely difficult to prove an insider dealing transaction in the stock markets. It is not easy to supervise insider dealing in stock markets because it’s very difficult to prove the insider trading transaction in terms of the intention of the trader and his knowledge of inside information.

Participant No. 3:

The only inside dealing that has been discovered is Bahbahani’s because it was very clear and it happened in stock markets while people were watching the agreement. It is extremely hard to supervise the transaction in stock markets to discover the crime.

Participant No. 4:

Written laws could be useless because the CMA departments did not adopt a policy to mitigate the insider trading risk. It is hard and difficult to prove the crime.

Participant No. 5:

Insider dealing is a crime that is hard to observe. How can the CMA supervise conversations taking place during a social event? At ‘Dwania’ [a place where men gather for social interaction] for example, inside information can be discussed, and based on that ‘others’ can choose to act. The only way that the CMA can observe insider trading in the stock markets is by ensuring that the trading is not before or after any announcement by the company, as it is a restricted period for insiders to trade in the stock markets, but there is much to improve.

Participant No. 6:

There is a way that insiders or even CMA staff can trade in stock markets without being caught, through an open trading account in a non-Kuwaiti company like one of the Gulf companies that trade online through a company like KMEFIC in Kuwait stock markets, so there is no way to trace the insider dealing. There is no mechanism in the CMA or Boursa to

discover the original investor, which is the insider who trades through online companies. The CMA must sign an agreement with Gulf Cooperation countries to exchange information about investors and companies.

The main point of identifying an insider is to ensure that he/she does not trade using inside information. Insiders are responsible for acting with honesty and integrity when dealing in stock markets.<sup>973</sup> It is the core duty of any director or employee of a listed company to protect the shareholders and the company's interest by ensuring equal access to information and not using unpublished price-sensitive information in pursuit of private gain.<sup>974</sup> The insider must maintain the confidentiality of inside information of which he/she becomes aware by virtue of his/her position or professional or personal relationships.<sup>975</sup> Additionally, the insider is obliged to maintain the confidentiality of data and information related to clients of a listed company, and shall not use or exploit these data or information.<sup>976</sup>

There is another important note: publication of inside information will not immediately influence prices of shares in the stock market. Generally, it takes some time to disseminate disclosed information to market participants. Accordingly, insider trading regulation prevents insiders from engaging in transactions for a period of time until the market adjusts after the release of inside information.<sup>977</sup> This means that an insider cannot trade in the stock market using inside information immediately after the announcement of the information to the regulator and the public,<sup>978</sup> but must wait until prices adjust in reaction to the information. This important concept is adopted in the UK approach, which does not allow insiders to deal immediately on stock markets after the announcement of inside information.<sup>979</sup> The CJA 1993 states in detail the procedures an insider must follow to trade in stock markets. It sets out 'made public' procedures to give clarity to insiders so they know when they are allowed to trade.<sup>980</sup> Enforcing a disclosure obligation is not enough to protect the market's integrity from insider trading:

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<sup>973</sup> Executive Bylaws, Module ten, Chapter three, Article 3-3.

<sup>974</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700) 5.

<sup>975</sup> Executive Bylaws, Module ten, Chapter three, Article 3-3-1.

<sup>976</sup> *ibid.* Article 3-3-3

<sup>977</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700) 44.

<sup>978</sup> The IOSCO, 'Insider Trading How Jurisdiction Regulate It', (2003) available at <<  
<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf>>> accessed 18 March 2020. 22.

<sup>979</sup> The CJA 1993.

<sup>980</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700) 44.

insiders can still benefit from inside information if their trading takes place immediately after an announcement. It is a positive development to impose a waiting phase on insiders until prices have adjusted to the new information. The law obliging listed companies to disclose inside information is designed to provide equal access to such information and prevent insider trading. The situation poses the question of when the regulator considers that the information is available to the public. The UK approach allows a waiting phase between disclosure to the regulator and the listed company's announcement, either in a press conference or in newspapers and the insider trades in stock markets.<sup>981</sup> It aims to ensure that market participants can react to the new price-sensitive information that a listed company has published.

Kuwait does not make any provision for waiting a reasonable time after disclosure of material information. This point is linked to the uncertainties of making inside information public. Restriction periods are imposed on insiders on only two occasions.<sup>982</sup> First, an insider cannot trade in stock markets for ten working days before the end of each quarter of the financial year, until the announcement of the financial results for that period. Secondly, an insider cannot trade for ten working days after the end of the financial year, until the announcement of the financial results for that year. It is clear that any stock market transaction by insiders is forbidden during the restriction periods, but what if the insider encourages or advises another person to trade during this time? The information is already public in the second situation (a restriction period after the announcement of financial results). In other words, despite restriction periods, insiders can still deal on the basis of inside information indirectly through encouraging or advising another person to trade during these periods. Kuwait's rule-based insider trading regulation needs amending to capture this misconduct.

There are two exceptional cases where an insider can trade in stock markets: first if he/she obtains approval to trade from the CMA,<sup>983</sup> and second if the insider faces any of the following unusual circumstances.<sup>984</sup>

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<sup>981</sup> Mohammad AlMutairi, above (n 24) 79.

<sup>982</sup> Executive Bylaws, Module ten, Chapter three, Article 3-4-1.

<sup>983</sup> Abdualla AlHayyan and Moahamad AlMuatari, above, (n 68) 696., Executive Bylaws, Module ten, Chapter three, Article 3-4-1-2.

<sup>984</sup> Executive Bylaws, Module ten, Chapter three, Article 3-4-1-3.

- a. Transfer of ownership as a result of inheritance or will.
- b. Dealing in Securities pursuant to a judicial judgment.
- c. Transfer of ownership from and to or among the Investment Portfolios managed by the licensed companies, provided that such is solely in favour of the beneficial owner.
- d. Transfer of ownership among spouses and Relatives up to the second degree.
- e. Subscription on Pre-emptive Rights of Securities or dispose of the same.
- f. Purchase of the required number of Shares to guarantee membership of the Board of Directors pursuant to the company contract.
- g. Transfer of ownership to settle a debt with a financial institution.
- h. Entering into a Merger or Acquisition Offer.
- i. Pledge of Securities.
- j. Transfer of ownership from the Listed Company to the employee in execution of the Securities purchase option plans.

These circumstances are limited in law to a few examples set out by the legislator to ensure that insiders do not generally use this excuse to trade.<sup>985</sup> But regardless of the two exceptional cases, the vital restriction on insiders dealing in stock markets is to protect the markets from insider trading. It is thus suggested that the current restriction period should be reformed to forbid insiders from dealing for period of time immediately after the announcement of material information.

The risk-based approach sets a strategy for supervising listed companies and uncovering insider trading in stock markets. To mitigate risk, the CMA can adopt various methods to prevent insider trading.<sup>986</sup>

#### 4.1 Performing additional enhanced checks as part of the authorisation function

The level of information that the CMA requires should be increased to prevent insider trading. For example, in Kuwait there is an ongoing merger between two of the largest banks, Kuwait Finance House and Bahrain's Ahli United Bank.<sup>987</sup> The market capitalisation of this merger is approximately £5 billion, according to Refinitiv data and

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<sup>985</sup> *ibid.*, Article 3-4-1-3.

<sup>986</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 18 March 2020.

<sup>987</sup> CNBC newspaper available at << <https://www.cnbc.com/news/view/49419/program/43>>> accessed 18 March 2020.

Reuters' calculation.<sup>988</sup> The CMA must impose additional obligations on these banks to prevent any leak of information that might be caused by the merger. It is important to focus the CMA's resources on supervising this ongoing merger because it has a high potential for insider trading. Additional information can include personal interviews, background checks and criminal records checks. For example, if any of the board of directors has a criminal record for insider trading, the CMA must take necessary steps to focus its resources on that person, either by demanding additional documents and information or by a face-to-face meeting. The risk-based approach sets a policy of limiting risk by focusing attention and resources on the individuals with the highest potential for committing an insider trading offence.

#### 4.2 Adjusting the type of insider trading supervision

There are different types of supervision, either off site or on site. Off-site supervision alone is insufficient in higher-risk situations:<sup>989</sup> both types are needed to tackle high-risk transactions. In the case of the ongoing bank merger in Kuwait, the CMA should undertake expected and unexpected on-site visits to investigate records and files and request further information. In this respect the CMA has appropriate powers:<sup>990</sup> CMA staff have judicial power to oblige listed companies to provide documents and agreements even if they are confidential.<sup>991</sup> But although the CMA has the investigative power, there is no published or express policy on how it should use on-site or off-site supervisions. It wastes time and money if resources are not focused on the higher risks and their potential to impact on the CMA's objectives. The current situation needs to be improved to set priorities based on the greatest risks.

#### 4.3 Adjusting thematic supervision

The CMA's supervisory decisions must use periodic reviews and whistleblowing to build a thematic map for focusing its resources. The combination of all obtained

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<sup>988</sup> Reuters available at << <https://uk.reuters.com/article/uk-aub-m-a-kuwait-finance-house/kuwait-finance-house-offers-17-percent-premium-in-merger-deal-with-bahrains-aub-idUKKCN1PI1UX>>> accessed 18 March 2020.

<sup>989</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 3 February 2020.

<sup>990</sup> The Executive Bylaws, Module 3, Chapter 2, Article 2-2

<sup>991</sup> *ibid.* Article 2-4

information creates a path for the CMA to follow in terms of the highest potential risks to its objectives.

#### 4.4 Adjusting the intensity of insider trading supervision

The risk-based approach facilitates answering the important question of how much resources and time the CMA should devote to a particular listed company. The level of supervision should be determined in line with the identified risks to provide adequate procedures to tackle insider trading. Intensive supervision includes due diligence, internal and external audit reports and interviews; it can wave a red flag regarding disorganised companies and those with insufficient controls in place, and make them take necessary steps to amend their weaknesses.

These methods are examples of how the financial regulator creates a framework for supervising listed companies.<sup>992</sup> The framework to mitigate risk must be updated and developed as necessary based on supervisory findings.

### **5. Insider trading supervision of securities in a cross-border context**

Effective supervision must take into consideration the different jurisdictions involved in insider trading. For example, the aforementioned ongoing bank merger required the CMA to review banks in both Kuwait and Bahrain. It is important for the supervisor in the home jurisdiction to have access to the customer, account and transaction data maintained by the financial institution in the host jurisdiction.<sup>993</sup> Both jurisdictions must set a framework to provide access to information, including suspicious trading reports, to assess a company's risk. Another example is a company with branches in different countries and registered on their stock markets: the home jurisdiction should be able to communicate with the host jurisdictions to exchange information. This is one of the weaknesses in Kuwait's CML regulation, because currently there is no adequate framework to exchange information about listed companies or clients. The CMA is

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<sup>992</sup> FATF, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 18 March 2020.

<sup>993</sup> *ibid*



currently in the process of signing an agreement about communication with other jurisdictions to exchange information, as Participant No. 5 confirmed:

The CMA is in a process of signing a memorandum of understanding about the protection of privacy data with European countries to provide more channels to exchange information about foreign investors. This agreement will allow Bursa and the CMA to ask for background checks about any foreign investor.

Lack of communication between securities regulators facilitates insider trading. It is necessary to ensure that there is coordination between the regulators, especially in Gulf countries, to exchange information and detect insider trading. Although the nature of trading has become more global, the detection, investigation and enforcement of market abuse offences are still undertaken by regulatory agencies at a national or even subnational level.<sup>994</sup> The scope of a particular agency's powers limits its detection and investigative capabilities, and may result in the agency not being able to make the necessary connection between, for example, an insider in its jurisdiction and a person outside the jurisdiction who trades on the basis of inside information obtained from this insider. Some of these difficulties may be addressed by enacting legislation to extend the extraterritorial reach of the agency's jurisdiction and powers, but this by itself is unlikely to be sufficient. The involvement and cooperation of other agencies are often required for effective detection of instances of market abuse which span more than one market or jurisdiction.

It helps to build a risk profile for every listed company in the stock markets, as required by a risk-based approach. The setting up of risk profiles gives the CMA a comprehensive view of the listed companies and enables it to allocate resources to high-risk companies.

## **6. Conclusion**

Kuwait's anti-insider trading regime has not set clear rules and a framework to regulate the crime. There is a lack of clarity in establishing the legal responsibilities of insiders in listed companies. These deficiencies affect the production of risk assessments to mitigate insider trading risk. The unclear definitions of 'inside information' and

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<sup>994</sup> Janet Austin, above, (n 951) 281.

‘insider’ are two main factors in establishing liability in insider trading crimes. The regulator’s risk-based approach and its reasons and effects must be fully understood and applied by all relevant departments, including those dealing with disclosure, trading and enforcement.

There are six significant contrasts between Kuwait and the UK regarding insider dealing that help to explain why the regimes operate differently, and these are also at the root of some of the recent divergences in case law between the two countries in this area. First, Kuwait only recognises the criminal regime to tackle and prevent insider trading in stock markets, while the UK has criminal and civil regimes to regulate insider trading. This is the most important aspect of differentiation between the Kuwaiti and UK systems.

Secondly, Kuwait does not provide a clear definition of insider trading as a crime, and its rule-based approach is an obstacle to the regulation of insider trading thanks to its inflexible rules. There is lack of clarity in acknowledging insider trading to be a crime, and no programme to train CMA staff or industry participants about such trading. It is suggested that a programme should be established between the CBK and the CMA to train their staff and the industry about the crime and its impact on the Kuwait stock markets.

Furthermore, Kuwait faces general obstacles in terms of judicial interpretation. The UK regime has largely evolved through judicial interpretation, which has led to a gradually developing body of common law and precedent around this topic and some elements of the concept of insider dealing being open to interpretation as a result. By contrast, the Kuwait regime is largely rule-based, with a series of specific offences being created and developed through primary legislation alone.

Thirdly, the uncertainties in the inside information definition affect the ability to identify risks to regulate insider trading. It is necessary to ensure agreement about the inside information definition and how it reflects on listed companies in stock markets. There is a need to increase awareness of the regulator’s approach to enable the industry to understand the importance of having dialogue and communication with the CMA.

Fourthly, although the CMA developed its insider definition after the 2015 CML amendments, there is still weakness. The CMA should include juristic persons as insiders with a legal responsibility to pay fines in cases of insider trading that benefits the company. The types of insiders must be clear and distinct from each other to allow imposition of the appropriate punishment.

Fifthly, the prohibited activities can be made more flexible to cover encouraging and advising another person to trade based on inside information. The territorial scope of an insider trading offence needs to be wide to give effective protection to domestic stock markets. There is no doubt that the CMA needs wider power to capture insider transactions committed outside Kuwait's territory. The legislative branch should be asked to reform the current insider trading regime, as this is the only way to amend Kuwait's rule-based regulation.

In terms of mitigation of insider risk, the CMA must set rules and regulations to implement its policy in the markets. It is important to ensure that there is an underlying strategy to focus resources on supervising the highest-risk companies. The CMA must oblige listed companies to provide additional documents and reports about any unusual trading in stock markets and suspicion transactions to establish effective supervision.

Finally, the lack of communication between CMA departments and supervisory authorities in terms of information about individuals and companies needs to be rectified immediately. Any lack of information is detrimental to the risk-based approach to optimising allocation of the CMA's resources.

## Chapter 8: Whistleblowing Regime

### 1. Introduction

Whistleblowing is a method to expose wrongdoing in both private and public sectors by allowing individuals to draw attention to misconduct in their organisations to protect the public interest.<sup>995</sup> The wrongdoing could include any type of misconduct, illegal activities or misbehaviour in financial services and stock markets. A whistleblowing regime promotes accountability to protect the public interest, and is essential to safeguard stock market integrity by preventing insider trading.<sup>996</sup> Whistleblowing can be defined as ‘the disclosure by organization members (former or current) of illegal, immoral, or illegitimate practices under the control of their employers, to persons or organization that may be able to effect action’.<sup>997</sup> There is no role model for constructing a whistleblowing regime in the financial sector:<sup>998</sup> each jurisdiction has its own framework and mechanism according to its system and culture. Even developed countries such as the UK<sup>999</sup> and US face difficulties in implementing an effective whistleblowing regime.<sup>1000</sup>

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<sup>995</sup> Jonathan Macey, 'Getting the Word Out About Fraud: A Theoretical Analysis of Whistle-blowing and Insider Trading' (2006) 105 Michigan Law Review 1899, 1903-1904.

<sup>996</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 5 February 2020.

<sup>997</sup> Janet Near and Marcia Miceli, 'Organizational Dissidence: The Case of Whistle-Blowing' (1985) 4 Journal of business ethics 1, 4 See also Janet Near and Marcia Miceli, 'Effective-Whistle Blowing' (1995) 20 Academy of management review 679. 680.

<sup>998</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 5 February 2020.

<sup>999</sup> In 2012, the Parliamentary Commission on Banking Standards (PCBS) was established to suggest recommendation for legislative to reform law. One of this recommendation to ensure more effective support for whistleblowers in the banking sector. Alexandra Webster, 'Developments in whistleblowing' (2015) 16 Business Law International 65, 66. See also MOORE, P. 2009a. House of Commons Treasury Select Committee Written Evidence Banking Crisis. MOORE, P. 2009b. Memorandum of Further Additional Evidence to the House of Commons Treasury Select Committee relating to the banking crisis MOORE, P. 2010.(Interview) Corporate governance and regulation of banks. Thirsk, Yorkshire. 10 July 2010. 1300 hrs.

<sup>1000</sup> Peter Yeoh, 'Whistleblowing: Motivations, Corporate Self-Regulation, and the Law' (2014) 56 International Journal of Law and Management 459, 460.

The Walker<sup>1001</sup> and Turner<sup>1002</sup> Reviews in 2009 highlighted that one of the major causes of the 2008 financial crisis in the UK was excessive and reckless risk-taking, so the UK reformed its legislation to adopt a more effective whistleblowing regime to avert future crises.<sup>1003</sup> Some jurisdictions require whistleblowers to report misconduct externally, while others require the misconduct to be reported internally for managers to take action.<sup>1004</sup> Whistleblowing can be seen as an internal management tool to protect the public from wrongdoing.<sup>1005</sup> it uses the right to free speech to highlight wrongdoing to a superior authority for it to take the necessary action,<sup>1006</sup> and enhances investor trust in stock markets.<sup>1007</sup> This research focuses only on whistleblowing related to insider trading in stock markets, and on reporting such wrongdoing to the external and superior authority in Kuwait's financial sector, the CMA.

There is a relationship between the type of wrongdoing and individuals' action to reveal misconduct in the organisation.<sup>1008</sup> For example, employees do not whistleblow wrongdoing if they believe nothing can be done to fix it or it is too risky to reveal the wrongdoer.<sup>1009</sup> The absence of appropriate protection in law exposes whistleblowers to risks of retaliation and criminal and civil liabilities. The challenge is achieving a regime that encourages individuals to blow the whistle on their organisations or colleagues while providing them with full protection.<sup>1010</sup> Thus whistleblower protection is one of the important elements in an effective regime.

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<sup>1001</sup> David Walker, 'A Review of Corporate Governance in UK Banks and other Financial Industry Entities' (November 2009) available < [https://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/walker\\_review\\_261109.pdf](https://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/walker_review_261109.pdf)> accessed 18 March 2020.

<sup>1002</sup> FSA, 'The Turner Review, A Regulatory Response to the Global Banking Crisis' (March 2009) available at <[http://www.actuaries.org/CTTEES\\_TFRISKCRISIS/Documents/turner\\_review.pdf](http://www.actuaries.org/CTTEES_TFRISKCRISIS/Documents/turner_review.pdf)> 22 January 2020

<sup>1003</sup> Alison Lui, 'Protecting whistle-blowers in the UK financial industry' (2014) 11 International Journal of Disclosure and Governance 195,196-197.

<sup>1004</sup> Jonathan Macey, above, (n 995) 1903.

<sup>1005</sup> Ronald Francis and Anona Armstrong, 'Corruption and whistleblowing in international humanitarian aid agencies' (2011) 18 Journal of Financial Crime 319, 332.

<sup>1006</sup> Faisal Al-Haidar, 'Whistleblowing in Kuwait and UK against corruption and misconduct' (2018) 60 International Journal of Law and Management 1020, 2.

<sup>1007</sup> Janet Near and Marcia Miceli, 'Effective-Whistle Blowing', above (n 997) 702.

<sup>1008</sup> Mark Somers and Jose Casal, 'Type of Wrongdoing and Whistle-Blowing: Further Evidence that Type of Wrongdoing Affects the Whistle-Blowing Process' (2011) 40 Public Personnel Management 151, 160.

<sup>1009</sup> *ibid.*

<sup>1010</sup> David Banisar, 'Whistleblowing: International standards and developments', in Irma, E. (Ed), Corruption and Transparency: Debating the Frontiers between State, Market and Society, (2001) World

An effective whistleblowing regime is part of international ethical governance to enhance the individual's role in helping to protect the soundness and safety of stock markets. International organisations such as the World Bank, the World Trade Organization, the OECD<sup>1011</sup> and IOSCO highlight the importance of proactive reporting by whistleblowers to protect the public interest.<sup>1012</sup> In 2011 the OECD provided guidance for legislators to create sufficient and effective whistleblower protection laws.<sup>1013</sup> Furthermore, the United Nations Convention against Corruption, Article 33, recommends that parties to the convention consider incorporating 'appropriate measures to provide protection against any unjustified treatment for any person who reports [offences] in good faith and on reasonable grounds'.<sup>1014</sup> This shows that adequate whistleblower protection is fundamental for an effective regime.

This chapter discusses whistleblowing in Kuwait to evaluate the detection of insider trading in stock markets in comparison to best practices in international organisations and the UK to reveal the deficiencies in the Kuwaiti system. It means that competent authorities must identify, assess and understand insider dealing risks to which they are exposed, and implement the most appropriate mitigation measures to focus their resources where the risks are higher.<sup>1015</sup> The chapter argues that there are weaknesses in the legislative framework of the whistleblowing regime, with a lack of clarity in the rules for insider trading in particular; narrow and restrictive reporting procedures to receive information about insider trading; inadequate protection for whistleblowers; a lack of implementation of existing international standards; a lack of available data on

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Bank Institute for Social Research, Washington, DC, 7-51. See also Jonathan Macey, above (n 995) 1899.

<sup>1011</sup> Peter Yeoh, above, (n 1000) 462.

<sup>1012</sup> Principle 8 of IOSCO objectives and standards IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > accessed 8 July 2019. See also IOSCO 'Credible Deterrence In The Enforcement Of Securities Regulation' June 2015 available at <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD490.pdf>> accessed 9 July 2019

<sup>1013</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 9 July 2019

<sup>1014</sup> UNCAC 'United Nations Convention Against Corruption' Available at <<<http://www.nazaha.gov.kw/EN/DocLib/UNITED%20NATIONS%20CONVENTION%20AGAINST%20CORRUPTION.pdf>>> accessed 14 February 2020.

<sup>1015</sup> FATE, 'Guidance for a Risk-Based Approach for the Securities Sector' October 2018 <<https://www.fatf-gafi.org/publications/fatfrecommendations/documents/rba-securities-sector.html>> accessed 3 February 2020.

whistleblowing reports; and a lack of public awareness of the whistleblowing regime in stock markets.

Before analysing the whistleblowing regime in Kuwait, it is useful to provide a brief background of the regime.

### 1.1 Brief background of Kuwait's whistleblowing regime

Two main laws regulate whistleblowing in Kuwait. First are the CML Executive Bylaws,<sup>1016</sup> issued in November 2015 to provide rules for whistleblowing violations and crimes in the financial sector.<sup>1017</sup> They set out procedures for reporting any crime in stock markets. The Executive Bylaws went through much discussion and amendment to reach their final form. The CMA used an online survey to obtain public comments and feedback on the new regulations. Any breach in the financial sector, including insider trading, is subject to the CMA's authority to receive a whistleblowing report and investigate the crime.

Secondly, the Anti-Corruption Law covers corruption crimes in Kuwait, and is applicable if the insider trading relates to crimes such as money laundering (discussed in the next section). The Anti-Corruption Law can be traced to Law No. 24 of 2012 on Establishing the Kuwait Anti-Corruption Authority and the Provisions on Disclosure of Assets and Liabilities (2012 Law). The 2012 Law established the Kuwait Anti-Corruption Authority (Nazaha<sup>1018</sup>) to receive whistleblower reports about any corruption crimes in Kuwait.

The 2012 Law had been in place for only a few years when the Constitutional Court issued a judgment on 19 December 2015 abolishing it due to procedural errors during the issuing of the law. Hence the National Assembly issued Law No. 2 of 2016 on Establishing the Kuwait Anti-Corruption Authority and the Provisions on Disclosure of

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<sup>1016</sup> CMA Administration Decision No. 72 of 2015

<sup>1017</sup> The CML Executive Bylaws, Module 3, Chapter 3.

<sup>1018</sup> The Anti-Corruption Authority decided to use term 'Nazaha' as the official name of the authority. It means integrity.

Assets and Liabilities (Anti-Corruption Law) to correct these procedural errors.<sup>1019</sup> It contains the same provisions as the previous 2012 Law.<sup>1020</sup>

In the UK the Public Interest Disclosure Act 1998 (PIDA) regulates the whistleblowing system. The purpose of PIDA is to protect individuals who disclose information in the public interest.<sup>1021</sup> Under PIDA, the FCA is a 'prescribed person' to which workers may whistleblow about suspected wrongdoing they believe may have occurred, including crimes and regulatory breaches. Revealing such information is known as making a 'disclosure'.<sup>1022</sup> The FCA also has Suspicious Transaction and Order Reports (STORs) for actual or attempted insider dealing.<sup>1023</sup> STORs came into force in July 2016 under the EU Market Abuse Regulation.

However, it should be noted that whistleblowing regimes in general are new regulations, and it takes time to change the culture in a society to whistleblow on misconduct in the workplace. It is important to introduce a whistleblowing culture in stock markets to prevent insider trading.<sup>1024</sup> In Kuwait the CMA must play an active role to raise public awareness about whistleblowing in the financial sector<sup>1025</sup> to increase reporting of wrongdoing.<sup>1026</sup>

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<sup>1019</sup> Anti-Corruption Law No.2 of 2016 available at << [http://undp-aci.org/publications/Nazaha%20Law%20no%20of%202016%20-%20FINAL%20\(EN\).pdf](http://undp-aci.org/publications/Nazaha%20Law%20no%20of%202016%20-%20FINAL%20(EN).pdf)>> accessed 5 February 2020

<sup>1020</sup> The Constitutional Court Judgment No. 24 of 2015 available at << <http://www.law.gov.kw/interalpage.aspx>>> accessed 18 April 2019. See also AlAnba newspaper available at << <https://www.alanba.com.kw/ar/kuwait-news/611427/20-12-2015--المحكمة-تقضي-بعدم-دستورية-قانون-انشاء-هيئة-مكافحة-الفساد>>> accessed 18 March 2020.

<sup>1021</sup> Peter Yeoh, above, (n 1000) 462.

<sup>1022</sup> Public Interest Disclosure Act 1998, 43F. see also The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020.

<sup>1023</sup> Suspicious Transaction and Order Report regime available at << <https://www.fca.org.uk/markets/market-abuse/suspicious-transaction-order-reports>>> accessed 18 March 2020.

<sup>1024</sup> Michael Filby, 'The Enforcement of Insider Dealing under the Financial Services and Markets Act 2000' (2003) 24 Company Lawyer, 4.

<sup>1025</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <<<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf>>> accessed 18 March 2020.

<sup>1026</sup> Janet Near and Marcia Miceli, 'Organizational Dissidence: The Case of Whistle-Blowing', above (n 997) 992.



## 2. Scope and definition

Kuwait has two competent authorities to receive whistleblowing reports. The first is the CMA, which is responsible for receiving any report about financial crime in stock markets.<sup>1027</sup> It is good practice to charge a specialist authority like this to investigate whistleblowing reports.<sup>1028</sup> Some scholars argue that another authority, like Nazaha, should be appointed to receive whistleblowing reports about financial crime and the private sector in general,<sup>1029</sup> on the grounds that the CMA does not provide adequate protection for whistleblowers nor prevent retaliation against employees in listed companies. Having two superior authorities to investigate whistleblowing gives more credibility to the regime, but one suggestion is to have a superior joint committee between the CMA and Nazaha to receive insider trading whistleblowing reports. This would enhance public accountability for protecting market integrity, as the IOSCO Principles recommend.

The second authority is Nazaha, but in accordance with the Anti-Corruption Law its remit is limited to corruption crimes. Insider dealing and financial crime are not categorised as corruption.<sup>1030</sup> The only situation where individuals can report to Nazaha is when the insider trading relates to corruption crimes such as money laundering.<sup>1031</sup> For example, if a listed company is owned by the government, an employee can report attempted insider trading to Nazaha if the transaction is related to money laundering or funding terrorist activities. This limitation to corruption crimes affects the effectiveness of the whistleblowing regime, because Nazaha can only be used for certain types of crime but its whistleblower protections are better than those of the CMA. As safeguarding market integrity is fundamental to strong stock markets,<sup>1032</sup> it is important to categorise financial crimes, especially insider trading, as corruption crimes to create decent protection for investment in Kuwait.

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<sup>1027</sup> The CML Executive Bylaws, Module Three, Chapter Three, Article 3-1

<sup>1028</sup> Khalida Saad Hulmi, above, (n 777) 104 See also Adel AlManea, 'above' (n 9) 90.

<sup>1029</sup> Hussain Boarki, above (n 4) 606. Also Participant No. 3 stated that it is important to allow Nazaha to receive the whistleblowing reports about financial crime and private sector.

<sup>1030</sup> Anti-Corruption Law No.2 of 2016, Article 22 of the

<sup>1031</sup> Ibid.

<sup>1032</sup> Jonathan Macey, above (n 995) 1914-1915.

Another element supports adopting two external superior authorities to receive whistleblowing reports on financial crime. Powerful groups in stock markets may influence the CMA to launch a formal investigation.<sup>1033</sup> Having another authority like Nazaha, with no conflict of interest, helps to increase the accountability of the primary regulatory authority. Since the CMA is responsible for supervising listed companies, it has a continued relationship with them that may cause a conflict of interest. Kuwait is a small society in which groups with political influence can play a major role in changing CMA procedures against a reported company.<sup>1034</sup> In other words, certain companies have the power to influence the CMA to stop an investigation, hence it is extremely important to reform the Anti-Corruption Law to include financial crime as corruption crime so that Nazaha has the authority to receive insider trading whistleblowing reports.

The seven expert interviewees were divided between wanting Nazaha to receive whistleblowing reports about insider trading and insisting that the CMA should be the sole authority to receive such reports. Participant No. 3 confirmed that there are weaknesses in the whistleblowing regime in Kuwait, especially because Nazaha does not receive reports about insider dealing:

Nazaha is responsible to receive whistleblowing about corruption crimes only if the insider dealing is related to public funds and corruption crimes, when Nazaha will be able to receive whistleblowing reports. Nazaha must amend their law to receive any whistleblowing information about financial crimes, including insider dealing, because it's the most dangerous crime against the economy.

Participants Nos 1 and 2 insisted that Nazaha should not be the authority responsible for receiving reports of insider trading because it only deals with corruption crimes and there is no need to amend the law.

Participant No. 1 stated:

Nazaha should not have any role in receiving any complaints about insider dealing because it is not a specialised authority. The CMA is the relevant authority. First, their role is to receive complaints about corruption crime only, but recently they have received many complaints about insider trading that they should not. In my opinion, Nazaha can only investigate crimes that are related to public employees and public companies.

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<sup>1033</sup> Mohammad E Al-Wasmi, above (n 428) 42, 52, 264.

<sup>1034</sup> Ayman Al-Buloushi, above (n 274) 15.

Secondly, they do not have a team of specialists to receive and investigate complaints about insider dealing in stock markets.

Participant No. 2 also highlighted that Nazaha does not have qualified teams to investigate insider dealing in stock markets:

Nazaha does not have qualified teams to investigate financial crime; it needs more experienced investigators to investigate these crimes. Therefore the CMA is the responsible authority to receive any whistleblow about financial crime in the stock markets. Nazaha can receive a whistleblow if it is related to corruption crimes. One solution to improve Nazaha's ability to investigate financial crimes is adopting a joint programme with the CMA to understand financial crime and be in a position to investigate insider trading. It is necessary to give people more than one authority to report to when they want to blow the whistle on insider trading. Investors must have confidence in the whistleblowing regime to expose any illegal activities in the markets and ensure the procedures conducted by the superior authority are fair. Limiting the recipients of whistleblowing complaints to the CMA alone serves no purpose, thus it is important to amend the Anti-Corruption Law to include financial crimes as corruption crimes.

Nazaha and the CMA share the same goal of protecting the industry from any wrongdoing, but there is no cooperation to promote this policy or adopt new tools to receive whistleblowing reports. Cooperation and communication between the superior authorities are important to understand the whistleblowing system and develop procedures and policy.<sup>1035</sup> Participant No. 1 said, 'There is no cooperation between the CMA and Nazaha in terms of reporting or [the] whistleblowing system.' This underlines the insufficient whistleblowing procedures in financial markets.

Another weakness in Kuwait's regime is that there is no official guidance regarding whistleblowing of insider trading from either the CMA or Nazaha, hence the stock markets are unaware of the most effective tools available for their protection. Participant No. 5 confirmed that there is no serious effort by the CMA to increase employee and public awareness of the whistleblowing regime, and lack of this awareness affects the effectiveness of the regime. This leads to another issue: the absence of a whistleblowing culture in society to report insider trading. Participant No. 1 confirmed this. The UK

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<sup>1035</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > accessed 18 March 2020.

approach is to publish rules and guidance to ensure that there is an understanding of the whistleblowing system in stock markets.<sup>1036</sup>

Employees must be trained to notice any change in patterns of insider deals in stock markets. Awareness of a change in pattern is a key element in uncovering financial crimes.<sup>1037</sup> This awareness can be built by training employees and individuals in investment companies to understand legitimate trades so they are able to detect any illegitimate transaction.<sup>1038</sup> There is no requirement to train employees and individuals in Kuwait to understand their role in reporting illegal activities in stock markets. This lack of awareness and understanding is a weakness in the whistleblowing regime.

The UK FCA staff and listed companies' employees are required to undertake formal training about money laundering and factors that may indicate it.<sup>1039</sup> There is no such training programme in Kuwait for staff of either the CMA or listed companies. Although the CMA runs workshops to increase awareness about the CML in general, there is no specific training or workshop about the whistleblower's role in uncovering financial crimes.

Participant No. 5 confirmed this shortcoming in Kuwait's legal system:

The CMA did not make any efforts to increase people's awareness about the whistleblowing system in stock markets. I think that none of the CMA's workshops discussed whistleblowing and there is no published statement about CMA policy in terms of a whistleblowing system to encourage people to come forward and whistleblow insider dealing.

Participant No. 1 confirmed that there is no culture in Kuwaiti society to whistleblow about insider trading to the CMA:

People do not have the culture to whistleblow insider dealing either to the CMA or to Kuwait's Anti-Corruption Authority.

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<sup>1036</sup> FCA, 'FCA Introduces New Rules on Whistleblowing' dated 19 April 2016 available at <<<https://www.fca.org.uk/news/press-releases/fca-introduces-new-rules-whistleblowing>>> accessed 18 March 2020.

<sup>1037</sup> Richard Alexander, 'The Role of Whistleblowers in the Fight against Economic Crime' (2005) 12 *Journal of Financial Crime*, 131, 132. 133.

<sup>1038</sup> *ibid.* 132

<sup>1039</sup> EU Money Laundering Directive in 1991.

Participant No. 5 thought that the lack of a culture of whistleblowing to the CMA on insider trading is because people do not feel obliged to report and are reluctant to get involve in major events which might led to criminal proceedings:

I believe that employees and individuals are embarrassed to whistleblow any insider dealing because they are unaware of the whistleblowing system. I personally think that people do commit insider dealing based on rumours or incomplete information or insider information, even with rules and regulation to incriminate any of these activities. There is insider dealing in stock markets.

Furthermore, the CMA has not undertaken any survey to ensure that its staff and listed company employees understand the whistleblowing regime. The FCA uses surveys to monitor the markets and its ability to implement the whistleblowing regulations.<sup>1040</sup> This proves the researcher's argument that there is no clarity about financial crime in Kuwaiti stock markets and the CMA does not fulfil its role to increase awareness of the whistleblowing system. An effective whistleblowing regime needs to change the culture in society to encourage individuals to report any misconduct in their companies.<sup>1041</sup> Hence the CMA must adopt a programme to change the current culture regarding blowing the whistle on insider trading. It is also important to publish the CMA policy about the whistleblowing regime and provide examples and guidelines. The CMA must require listed companies to conduct formal training about financial crime in general and insider trading in particular.

## 2.1 Wrongdoing

Misconduct includes any illegal act or illegitimate organisational acts that can breach any provision of the CML and its Executive Bylaws.<sup>1042</sup> The purpose of whistleblowing is to expose misconduct and impose sanctions on wrongdoers. Any person knowing of a financial crime or violation of financial regulations must report the wrongdoing to the

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<sup>1040</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 5 February 2020.

<sup>1041</sup> Janet Near and Marcia Miceli, 'Effective-Whistle Blowing', above (n 997) 679.

<sup>1042</sup> The CML Executive Bylaws, Module 3, Chapter 3, Article 3-1.

CMA.<sup>1043</sup> This means the law has a wide definition of wrongdoing that includes any violation or crime in the stock markets, such as insider trading.

In contrast, Nazaha has a narrative approach to certain types of crime in reporting misconduct. The definition of corruption crimes covers the following.<sup>1044</sup>

1. Offences against the public funds stipulated in Law No. (1) for the year 1993 regarding the protection of public funds.
2. Bribery and abuse of influence stipulated in Law No. (31) for the year 1970 amending some provisions of the Penal Code No. (16) for the year 1960.
3. Crimes stipulated in Law No. (106) for the year 2013 regarding Combating Money-Laundering and the Financing of Terrorism.
4. Falsification and forgery offenses stipulated in law No. (16) for the year 1960 issuing the Penal Code.
5. Offenses relating to the administration of justice stipulated in law No. (16) for the year 1960 issuing the Penal Code.
6. Crimes of Illicit Gain stipulated in this Law.
7. Crimes of smuggling stipulated in Law No. (10) for the year 2003 issuing the Common Customs Law of the GCC [Gulf Cooperation Council] States.
8. Crimes of tax evasion stipulated in Decree No. (3) for the year 1955 regarding Kuwait Income Tax.
9. Crimes of impeding the work of the Authority, putting pressure upon it to hinder the performance of its duties, interfering in its terms of reference, or refraining from providing it with the required information stipulated by this law.
10. The crimes stipulated in Law No. (10) for the year 2007 regarding protection of competition.
11. The crimes stipulated in Law No. (25) for the year 1996 regarding the disclosure of commissions in connection with State contracts.
12. Any other crimes stipulated in other law, which are considered corruption offences.

Although this provision does not mention insider trading as a crime of corruption, it is included if the inside trading relates to another corruption crime like money laundering. However, neither the CMA nor Nazaha publishes official guidelines regarding whistleblowing on insider trading in stock markets.

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<sup>1043</sup> *ibid.* Article 3.

<sup>1044</sup> Anti-Corruption Law No.24 of 2012, Article 22.

In the UK the FCA uses the STOR regime to report any suspicion transaction in the markets. The FCA Handbook provides examples and clarification of what could be insider dealing,<sup>1045</sup> and guidelines to help market participants understand what it involves. PIDA stipulates that whistleblowing information should relate to misconduct that happened in the past, is happening now, or there is reasonable reason to believe will happen soon and which affects the public interest.<sup>1046</sup> Individuals can blow the whistle on any suspected wrongdoing they believe may happen in a company, including crimes and regulatory breaches. Thus the UK recognises both crimes that have already occurred and crimes that might happen in the future.<sup>1047</sup>

An important key weakness in Kuwait's whistleblowing regime is that it applies only to crimes that have been committed, and does not recognise attempted crimes or those that have yet to happen. Insider trading in stock markets needs time to be completed, because the insider waits until the inside information is public to get the benefit of the illegal action. Thus the timeline for insider trading differs from that for other crimes. Whistleblowers should be able to report attempted insider trading to ensure that Nazaha or the CMA can prevent the transaction. The inability to do this is a weakness in the legislative framework of the whistleblowing regime.

## 2.2 Whistleblowers

A whistleblower can be defined as 'an employee or other person in a contractual relationship with a company who reports misconduct outside firms or institutions, which in turn have the authority to impose sanctions or take other corrective action against the wrongdoer'.<sup>1048</sup> Whistleblowers can report wrongdoing internally or externally to the superior authority to have the crime investigated. The CML Executive Bylaws give a wide definition of whistleblowers in financial sectors: 'a person that submits a report'.<sup>1049</sup> This definition includes any person who hears about insider trading in stock

<sup>1045</sup> FCA handbook, SUP15 ANN5 available at <<<https://www.handbook.fca.org.uk/handbook/SUP/15/Ann5.html>>> accessed 18 March 2020.

<sup>1046</sup> UK Public Interest Disclosure Act 1998, Part IV.A., Section 43B, See also Whistleblowing for Employees << <https://www.gov.uk/whistleblowing>>> accessed 5 February 2020.

<sup>1047</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020.

<sup>1048</sup> Black's Law Dictionary (8<sup>th</sup> ed. 2004), see also Jonathan Macey, above (n 995) 1903

<sup>1049</sup> The CML Executive Bylaws, Module One, Glossary.

markets. It is recommended practice to have a broad definition to ensure that the responsibility to protect market integrity is the duty of every person in the financial industry<sup>1050</sup> – including participants’ wives, family members and housekeepers. It is a positive development to include all these people as being able to blow the whistle on insider trading, but the lack of awareness about whistleblowing procedures makes this tool useless to protect the market. Anti-Corruption Law Article 1 defines a whistleblower as ‘the person who reports any corruption offence. That also applies to the witnesses, victims of crimes and the experts who give testimony concerning criminalized acts.’ The definition limits the whistleblower’s role to reporting corruption crime only, not any breach of other laws that affect the public interest, but its wide definition of a whistleblower includes any person who reports misconduct in a company, including primary and secondary insiders and others.

The most important point is that whistleblowing must relate to misconduct by a member of the company who breaks the law. Hence the whistleblower must have knowledge and understanding of the trading process to be able to notice misconduct and illegal activities in the company. He/she must know the basic rules about trading in stock markets to have the knowledge to expose insider trading. It is no easy task to detect insider trading, because it is a sophisticated crime and takes someone with experience in the field to uncover the transactions.<sup>1051</sup> The CMA does not publish any guidance on how to discover insider trading, and most people are unaware of the fundamental rules in stock markets. The CMA needs to ensure that individuals understand whistleblowing rules. The credibility of the whistleblower is important to ensure that the CMA or Nazaha take action to investigate the wrongdoing.

Factors that might affect a whistleblower’s decision to reveal insider trading are his/her trust that the authority will do something to remedy the unethical or illegal activities, and confidence that he/she is protected. Some whistleblowers will not come forward to reveal wrongdoing because they believe that nothing will be done.<sup>1052</sup> Employees need to trust the authority to take serious action to prevent and punish the insider. This trust

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<sup>1050</sup> Principle 8 of IOSCO objectives and standards ‘Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation’ May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > > accessed 18 March 2020.

<sup>1051</sup> Barry Rider, Kern Alexander, and Lisa Linklater, above, (n 700)17.

<sup>1052</sup> Mark Somers and Jose Casal, above, (n 1008) 157.



must be built by publishing the whistleblowing policy and the outcomes reports produced by the CMA and Nazaha. Most importantly, the whistleblower should trust the procedures and understand that he/she will suffer no harm or punishment if the reported insider trading is not proved. It is important to guarantee the whistleblower legal protection against prosecution after reporting insider trading.

### **3. Mechanisms for protection**

One of the areas that international organisations identify as being a high priority in achieving an effective whistleblowing regime is the protection of whistleblowers.<sup>1053</sup> To encourage people to report insider trading it is essential to give them adequate protection from dangers that might arise if their identity is exposed.<sup>1054</sup>

The whistleblower protection laws are regulated by the CML and its Executive Bylaws for financial crimes in stock markets,<sup>1055</sup> and the Anti-Corruption Law<sup>1056</sup> for corruption crimes such as insider trading related to money laundering. The CMA and Nazaha provide different levels of protection. In the UK whistleblower protection falls under PIDA, which provides the legal framework for safeguarding whistleblowers from any harm.<sup>1057</sup>

#### **3.1 Protection against retaliation**

Whistleblower regimes must provide comprehensive protection against discriminatory or retaliatory personal action.<sup>1058</sup> The CMA and Nazaha do not list or give examples of employment-related reprisals, or provide any guidance to protect an employee from the employer's revenge. The only provision regulating such reprisals is broad, without any specification of what action should be considered as retaliation.<sup>1059</sup> There are general

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<sup>1053</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 18 March 2020.

<sup>1054</sup> Janet Near and Marcia Miceli, 'Organizational Dissidence: The Case of Whistle-Blowing' above (n 997) 6-7. See also OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 18 March 2020.

<sup>1055</sup> Executive bylaws, Model 3, Chapter 3, Article 3-8

<sup>1056</sup> Anti-Corruption Law, Article 37-39

<sup>1057</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020.

<sup>1058</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 18 March 2020.

<sup>1059</sup> The CML Executive Bylaws, Module 3, Chapter 3, Article 3-9 and Article 3-10

rules about protecting whistleblowers from retaliation, but the whistleblower must prove the link between the whistleblowing and the administrative action.

In term of the burden of proof, the recommended practice is to oblige the employer to prove that any action taken against a whistleblower is unrelated to his/her report about wrongdoing.<sup>1060</sup> According to the provision, a whistleblower will be protected from any decision the employer takes in reaction to his/her reporting. This shifts the burden to the employer to prove that its decision was based on fair and reasonable grounds and unrelated to the whistleblowing. None of these good practices exists in Kuwait's whistleblowing regime, for either the CMA or Nazaha, which shows the weaknesses in the legislative framework for whistleblower protection.

In the UK PIDA provides protection to employees who report misconduct to serve the public interest.<sup>1061</sup> The whistleblower is protected by law and may not lose his/her job or be treated unfairly.<sup>1062</sup>

An employee who is dismissed shall be regarded for the purposes of this Part as unfairly dismissed if the reason (or, if more than one, the principal reason) for the dismissal is that the employee made a protected disclosure.<sup>1063</sup>

### 3.2 Criminal and civil liability

Whistleblower protection must include administrative, occupational and legal protection.<sup>1064</sup> Legal protection means the CMA and the government should not bring a criminal, civil or disciplinary case against the whistleblower.<sup>1065</sup> Individuals must be protected from criminal and civil sanctions if they disclose inside information that is considered as secret in a listed company.<sup>1066</sup> The legal protection should waive these

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<sup>1060</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 18 March 2020.

<sup>1061</sup> UK Public Interest Disclosure Act 1998 available at <<  
<http://www.legislation.gov.uk/ukpga/1998/23/contents>>> accessed 5 February 2020.

<sup>1062</sup> The Public Interest Disclosure Act 1998 available at <<  
<http://www.legislation.gov.uk/ukpga/1998/23/contents>>> accessed 5 February 2020. See also Whistleblowing for Employees << <https://www.gov.uk/whistleblowing>>> accessed 5 February 2020.

<sup>1063</sup> UK Public Interest Disclosure Act 1998, 5 103A available at << <https://www.pcaw.org.uk/a-guide-to-pida/>>> accessed 5 February 2020

<sup>1064</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 5 February 2020

<sup>1065</sup> *ibid.*

<sup>1066</sup> *ibid.*

criminal or civil sanctions or disciplinary decisions to allow individuals to report insider trading to the competent authority.

Legal protection is defined in the CML Executive Bylaws:<sup>1067</sup>

it is not permitted to charge a Whistle blower with criminal, civil or disciplinary charges as long as the Whistle blower thought in good faith that the incident he reported was appropriate to be reported in this context regardless of the result of the Report.

However, another provision in the law contradicts this:<sup>1068</sup> a whistleblower shall be subject to criminal, civil or disciplinary charges if he/she submits a report in contravention to the CML or any other law. This provision destroys the legal protection for whistleblowers: they will be subject to legal action if their report about insider trading violates the CML or any other law. The whistleblower cannot guarantee his/her protection because the article is vague and does not determine a specific action. ‘Other law’ could be many laws of which the whistleblower is unaware. As a result, people do not blow the whistle on insider trading because they cannot protect themselves from legal action. Inadequate protection for whistleblowers affects the effectiveness of the whole regime.

The Anti-Corruption Law has a similar provision which states that whistleblowers should be punished if the reported information is false, or they conceal data or information relevant to the report, or the report is fraudulent, or they mislead the judiciary.<sup>1069</sup> The punishment can be three years’ imprisonment and possible dismissal from their job.<sup>1070</sup> This significantly affects an employee’s decision to report misconduct in the workplace.

Furthermore, whistleblowers must truly believe in good faith that there is misconduct in the organisation that affects the public interest. The CML Executive Bylaws require

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<sup>1067</sup> The CML Executive Bylaws, Module 3, Chapter 3, Article 3-11

<sup>1068</sup> Faisal Al-Haidar, above, (n 1006) 5. See also The CML Executive Bylaws, Module Three, Chapter Three, Article 3-12. Also see Article 53 of Law No. 2 of 2016.

<sup>1069</sup> Anti-Corruption Law, Article 53

<sup>1070</sup> *ibid.*

the whistleblower to believe in good faith that the suspect undertook insider trading in stock markets.<sup>1071</sup> Anti-Corruption Law Article 65 states:

Anyone [who] believes, in the good faith, that the incident he reports is correct as he has serious indications justifying such reporting shall not be subject to any punitive, civil or disciplinary actions whatever the result of the report.

It seems that the CMA and Nazaha link good faith with whistleblower protection, but there is no definition of good faith. Insider trading is a complex crime that is hard to prove, and it is difficult to provide evidence of good faith. But if a person reports misconduct without giving an adequate reason for this belief and proving good faith, the whistleblower may be subject to legal action. This is further proof of inadequate whistleblower protection. First, it is hard to prove that a whistleblower submitted a report based on good or bad faith, especially regarding insider trading in stock markets. Whistleblowers must be experts in market transactions to uncover insider trading, as in the early stages it is difficult to prove. Secondly, the reason for whistleblowing is to provide the CMA with information to start investigating a crime. People will hesitate to report misconduct if there is a chance of being punished for such reporting. The CMA or a listed company can pursue a whistleblower with litigation if he/she fails to prove that his/her report was made in good faith.<sup>1072</sup> Insider trading is hard to prove, and there is no guarantee of the case succeeding after formal investigation. The whistleblower of a corruption crime might face prison if he/she fails to prove that a report of insider trading was based on good faith.<sup>1073</sup> Obviously, there is no implementation of existing international standards to provide adequate whistleblower protection.

It seems that the law limits protection to successful cases only. Individuals will be reluctant to report insider trading if they will be punished for taking action. It is suggested that the laws are reformed to provide more protection to whistleblowers by setting out a list of actions and legal protections to ensure that individuals have a clear idea of the consequences of their decision.

### 3.3 Anonymity and confidentiality

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<sup>1071</sup> The CML Executive Bylaws, Module Three, Chapter Three, Article 3-11

<sup>1072</sup> *ibid.* Article 3-11 and 12

<sup>1073</sup> Anti-Corruption Law, Article 53.

Anonymity is an important element in an effective whistleblowing regime.<sup>1074</sup> Keeping the whistleblower's identity confidential ensures that he/she and his/her family are protected and that whistleblowers are not treated unfairly or harmed in any manner because of their reports. An employee's decision to report insider trading might be affected by this consideration: it is risky to blow the whistle on wrongdoing if the wrongdoer has the capability to harm the whistleblower.<sup>1075</sup> Hence the whistleblowing regime should ensure that the whistleblower's identity can be covered and not traced by companies. This is crucial: if the protection programme is weak, whistleblowers will not be encouraged to report crimes. The importance of hiding the identity of financial whistleblowers is recognised in the CML Executive Bylaws:

The CMA may provide protection to the Whistle-blower through hiding their identity and identifying them only with special codes. The CMA shall prepare confidential records including the original data of one whose identity is decided to be hidden or is being protected. Records shall be maintained as confidential and shall be revealed only by a decision by the CMA or the Competent Court. The CMA may adopt any other measures or procedures it considers necessary to provide protection to a Whistle-blower or witness.<sup>1076</sup>

This provision suggests that the CMA 'may' provide protection, which means there is no obligation to hide the whistleblower's identity. This anonymity must be guaranteed by law and not left to the discretion of the CMA. The CMA will disclose a whistleblower's identity if the court requests this, without providing any guarantee to protect the whistleblower. There is no limit to the power of the CMA or the court to reveal a whistleblower's identity. In the UK the FCA tries to limit the potential damage by disclosing the whistleblower's name to the judge only;<sup>1077</sup> there is no such protection in Kuwait. Additionally, there are no internal procedures for methods to conceal the identity of the whistleblower, and no published policy in terms of thematic procedures to deal with this form of protection. The law stipulates this protection, but the CMA does not provide any instructions about how to guarantee whistleblower anonymity.

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<sup>1074</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 5 February 2020.

<sup>1075</sup> Mark Somers and Jose Casal, above, (n 1008) 160. See also Janet Near and Marcia Miceli, 'Organizational Dissidence: The Case of Whistle-Blowing' above (n 997) 6.

<sup>1076</sup> The CML Executive Bylaws, Module 3, Chapter 3, Article 3-8

<sup>1077</sup> The FCA report, 'How We Handle the Disclosures from Whistle-blowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 5 February 2020

Furthermore, the CMA does not impose a fine if a member of its staff exposes the identity of a whistleblower, and there are no sanctions to ensure whistleblower anonymity. Recommended international practice is to impose a penalty of imprisonment or a fine for revealing a whistleblower's identity.<sup>1078</sup>

Hiding a whistleblower's identity is in any case problematic. The whistleblowing report must include the whistleblower's personal information, such as name, address, phone numbers, position and signature.<sup>1079</sup> These details are mandatory, otherwise the CMA cannot accept the report. The CMA must change its rules to facilitate whistleblowers reporting any insider trading in stock markets without providing personal information, to encourage individuals to come forward and report crimes. The CMA must focus on the value of the reported information, not on the whistleblowers' identities. In the UK the FCA will try to assemble a whistleblower's information and investigate the wrongdoing without asking the informant for a face-to-face meeting.<sup>1080</sup>

Participant No. 4 highlighted the weakness in the CMA whistleblowing system and its strict conditions and requirements, which made it hard to implement:

There is a huge gap in the whistleblowing system in the financial sector. The only jurisdictions that have succeeded to regulate whistleblowing system are the US and UK. They encouraged people to whistleblow by publishing their policy and the purpose of the law. The whistleblower must inform the authority with new information that helps them to investigate. In Kuwait the whistleblower must provide sufficient evidence and personal details about the incident or the illegal activities. This condition damages the purpose of the whistleblowing system and discourages people to blow the whistle anonymously.

In contrast, under the Anti-Corruption Law Nazaha gives whistleblowers more personal protection to hide their identity than the CMA, providing a guarding escort and a new place of residence.<sup>1081</sup> The question is whether Nazaha's protection programme will be effective in a small country like Kuwait. It is not difficult to uncover the new residences of whistleblowers and their families. Kuwait's total population is 4,751,670, of whom

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<sup>1078</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 5 February 2020.

<sup>1079</sup> The CML Executive Bylaws, Module Three, Chapter Three, Article 3-2

<sup>1080</sup> The FCA report, 'How We Handle the Disclosures from Whistle-blowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 5 February 2020

<sup>1081</sup> Anti-Corruption Law, Article 41.

1,410,049 are Kuwaiti citizens,<sup>1082</sup> so it is a small society where people know each other by family names and have many connections, making it easy to find them. It is unrealistic to give a whistleblower and his/her family a new place of residence in Kuwait, and the result is that whistleblower protection in Kuwait is ineffective. The situation is totally different in the UK, which is a bigger country with many cities in which to relocate a whistleblower.

The limited protection in Kuwait's system affects how people react to insider trading in their companies. It is suggested that a risk-based approach is used to create different types of protection in Kuwait's whistleblowing regime, such that people facing the highest risks are entitled to have a new identity in another country. The categorisation will help to establish new whistleblower protection and gradually set rules to assist the highest-risk informers. It also helps to set priorities for paying immediate attention to the employees who are in greatest danger. This suggestion requires Kuwait to have an agreement with another country to facilitate the implementation of the system. International cooperation is helpful in whistleblower protection: the UK entered into arrangements with Australia and Canada to conceal whistleblowers by giving them new residences.<sup>1083</sup> Additionally, the CMA and Nazaha must work together to increase public trust in their ability to prevent and punish insider trading.

#### **4. Reporting procedures and mechanisms**

The whistleblower's role is only to report misconduct, not to investigate it.<sup>1084</sup> In some jurisdictions, like the US, if the fraud is successfully prosecuted the whistleblower is entitled to a financial reward,<sup>1085</sup> but the main purpose of a whistleblowing regime is to give the competent authority sufficient information to uncover a wrongdoing.

First, it is important to distinguish whistleblowing from other types of report. There is a difference between whistleblowing to expose misconduct and internal reporting to cover up misconduct. An example of the latter is a letter written by an Enron employee called Sherron Watkins, trying to cover up her involvement in illegal activities that led

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<sup>1082</sup> Kuwait Statistics Service System available at << <https://www.paci.gov.kw/stat/default.aspx> >> accessed 5 February 2020.

<sup>1083</sup> Richard Alexander, above, (n 1037) 133.

<sup>1084</sup> Alexandra Webster, above, (n 999) 66-67.

<sup>1085</sup> Jonathan Macey, above (n 995) 1906.

to the collapse of Enron.<sup>1086</sup> Sherron wrote a memorandum to explain her concerns about suspicions of accounting improprieties in the company, and addressed it the company's CEO.<sup>1087</sup> This memo was not reporting misconduct, but rather it was covering up her involvement in those activities.<sup>1088</sup> It is important to distinguish between whistleblowing and reporting to cover up misconduct to have an effective whistleblowing regime.

Secondly, whistleblowing is not blackmail: it does not involve covering up information in return for money,<sup>1089</sup> but aims to pass information regarding misconduct to the superior authority to punish the wrongdoer. Unlike blackmail, whistleblowing is not a deal to ensure that a non-compliant organisation 'gets away with it' and does not receive punishment for its wrongdoing.

Finally, whistleblowing is not a complaint.<sup>1090</sup> Although both types of reports include information about misconduct and illegal activities in a company, the whistleblower has no personal interest in the outcome of the investigation – unlike a complaint, where the employee hopes the outcome will bring some reward,<sup>1091</sup> such as promotion or a bonus. Personal gain should not be a motive to whistleblow on misconduct in the company, but this does not mean that the whistleblower is not entitled to receive reward.<sup>1092</sup>

#### 4.1 Conditions for making a disclosure

It is important to clarify that the main purpose of a whistleblowing regime is to provide the competent authority with information to enable it to take the necessary steps and detect wrongdoing. The key point is to protect the public interest in stock markets. The IOSCO Principles recommend that an effective whistleblowing regime for receiving information about illegal activities is essential for strong markets.<sup>1093</sup>

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<sup>1086</sup> Jonathan Macey, above (n 995) 1909.

<sup>1087</sup> Ibid. 1907.

<sup>1088</sup> Ibid. 1907-1908.

<sup>1089</sup> Ibid. 1938.

<sup>1090</sup> Faisal Al-Haidar, above, (n 1006) 3.

<sup>1091</sup> Peter Yeoh, above, (n 1000) 462.

<sup>1092</sup> Richard Alexander, above, (n 1037) 133.

<sup>1093</sup> IOSCO 'Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation' May 2017 <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD562.pdf> > > accessed 19 February 2020.



The UK implements this recommendation by adopting a fair basis for considering whistleblowing reports. In accordance with EU Market Abuse Regulation Article 16(1)–(2), listed companies are required to establish an effective arrangement, system and procedures for detecting and preventing actual or attempted market abuse, and report incidents to competent authorities (the FCA in the UK) without delay.<sup>1094</sup> Individuals must submit reports if there are reasonable suspicions of actual or attempted insider dealing either in the past or in the future.<sup>1095</sup> The competent authority might ask for further explanation and information about the reported misconduct. The suspected transaction must be based on reasonable grounds that it might constitute insider dealing,<sup>1096</sup> and whistleblowers must reasonably believe that the information is true when informing the FCA.<sup>1097</sup> There are certain conditions to qualify the information as whistleblowing: PIDA refers to ‘any disclosure of information which, in the reasonable belief of the worker making the disclosure, tends to show one or more of the following...’ – the provision continues by listing a series of acts, including in relation to the commission of criminal offences.<sup>1098</sup>

Kuwait also requires reasonable grounds to blow the whistle on insider trading. The whistleblower must have a decent and reasonable belief that the reported misconduct took place, and provide a sufficient basis to determine who bears the responsibility for the misconduct.<sup>1099</sup> This is critical point in distinguishing between whistleblowing and rumour, where no one is held to account. In Kuwait the whistleblower should have reasonable grounds, but also must provide credible evidence to prove insider dealing in stock markets:

It is a condition that a Report of a crime or Violation stipulated in the Law shall be based on credible evidence which justifies a Whistle blower’s

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<sup>1094</sup> Article 16 of Suspicious Transaction and Order Report regime available at << <https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-1402-EN-F1-1.PDF>>> accessed 5 February 2020.

<sup>1095</sup> FCA handbook, SUP15.10 available at << <https://www.handbook.fca.org.uk/handbook/SUP/15/10.html?date=2016-06-17>>> accessed 5 February 2020. See UK Public Interest Disclosure Act 1998, Part IV.A., Section 43B (1). See also Whistleblowing for Employees << <https://www.gov.uk/whistleblowing>>> accessed 5 February 2020.

<sup>1096</sup> FCA handbook, SUP15.10 available at << <https://www.handbook.fca.org.uk/handbook/SUP/15/10.html?date=2016-06-17>>> accessed 5 February 2020.

<sup>1097</sup> Michael Filby, above, (n 1024) 4-5.

<sup>1098</sup> UK Public Interest Disclosure Act 1998, Part IV.A., Section 43B.

<sup>1099</sup> Faisal Al-Haidar, above, (n 1006) 2

reasonable belief of the reported incident. A Report shall not be considered if it is without documentary or other evidence in justification.<sup>1100</sup>

The provision does not require just any evidence: it must be credible evidence. However, no guidelines or clarification are provided to determine what should be considered as credible evidence. This approach should not be used for insider trading, because a whistleblower does not necessarily have documents to support the report of illegal activities. The whistleblower's role should only be to report information about insider trading, and it is the CMA's responsibility to investigate the crime. The current provision shifts the burden of proof to the whistleblower, which in practice is inapplicable and weakens the whistleblowing regime. Narrow and restrictive conditions for reporting information about insider trading make the regime ineffective. An effective risk management system requires regulation to be flexible and capable of detecting any attempted insider trading.

The FCA encourages people to provide any information about potential risk, including insider dealing,<sup>1101</sup> then follows up the information and asks the listed company to provide clarification if necessary.<sup>1102</sup> In some cases the FCA pieces the whistleblowing report together with information from other sources to take action. In other words, it is not the whistleblower's role to establish legal responsibility and prove the wrongdoing.

Participant No. 4 highlighted the weaknesses in the Kuwaiti whistleblowing mechanism and procedures in requiring such strict conditions:

There is no clear mechanism for whistleblowing in stock markets. Article 3.2 of the CML Executive Bylaws deals with how a person can whistleblow or report a financial crime with such strict requirements as stated by the law. The requirements are impossible to fulfil. It requires the whistleblower to provide sufficient evidence and provide his information and so many conditions just to accept his whistleblow report. It is clear that the regulator did not understand the purpose of the whistleblowing system to highlight wrongdoing in the stock markets, to allow the CMA to do further investigation to discover the crime. It seems that there is confusion between whistleblowing and a complaint that a person with personal interest must file.

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<sup>1100</sup> The CML Executive bylaws, Module 3, Chapter 3, Article 3-1

<sup>1101</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020.

<sup>1102</sup> *ibid.*

The ability to provide a legitimate channel to report insider trading is important in an effective whistleblowing regime. Whistleblowing laws refer to one or more channels by which protected disclosures can be made,<sup>1103</sup> generally including both internal and external disclosures. Employees should report insider trading internally before going to an external authority.<sup>1104</sup> The appropriateness of internal disclosure depends on the company itself:<sup>1105</sup> companies must create a good environment and impose internal rules to ensure that employees are encouraged to speak out about wrongdoing internally.<sup>1106</sup> There are mechanisms in companies to ensure appropriate protection for whistleblowers. The bureaucratic structure of the company determines how it will respond to a wrongdoing: a less bureaucratic organisation will encourage employees to report insider trading.<sup>1107</sup> Listed companies should have internal compliance management systems to ensure there is no violation of the law and employees are encouraged to report any crimes in stock markets, like the UK approach.<sup>1108</sup> This helps to create a good environment and encourage whistleblowing, but not every listed company supports this approach. It depends on the listed company itself, and whether misconduct is part of its profit-making strategy.<sup>1109</sup> In other words, some companies rely on wrongful acts to do business and continue to perform well in the markets. Medium-sized companies might use misconduct to survive in difficult times,<sup>1110</sup> but large companies generally cannot depend on wrongdoing to do business.

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<sup>1103</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 6 February 2020.

<sup>1104</sup> Alison Lui, above, (n 1003) 8. See also MOORE, P. 2009a. House of Commons Treasury Select Committee Written Evidence Banking Crisis. MOORE, P. 2009b. Memorandum of Further Additional Evidence to the House of Commons Treasury Select Committee relating to the banking crisis MOORE, P. 2010. (Interview) Corporate governance and regulation of banks. Thirsk, Yorkshire. 10 July 2010. 1300 hrs. See Article 16 of Suspicious Transaction and Order Report regime available at <<<https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-1402-EN-F1-1.PDF>>> accessed 5 February 2020.

<sup>1105</sup> Janet Near and Marcia Miceli, 'Effective-Whistle-Blowing', above (n 997) 681, 686-687, 698-699.

<sup>1106</sup> Michael Filby, above, (n 1024) 5.

<sup>1107</sup> Janet Near and Marcia Miceli, 'Effective-Whistle Blowing', above (n 997) 701-702. See also Alison Lui, above, n414, 8-11, 14.

<sup>1108</sup> Ibid, 8-14, See also Michael Filby, above, (n 1024) 5.

<sup>1109</sup> Janet Near and Marcia Miceli, 'Effective-Whistle Blowing', above (n 997) 687.

<sup>1110</sup> Ibid.,

The CMA requires listed companies to adopt the governance regulation and set out a code of conduct, including internal whistleblowing procedures.<sup>1111</sup> The governance regulation does not set minimum standards or procedures for internal whistleblowing, and the policies in listed companies give no detailed information to employees who want to do so. The code of conduct must include details on how to protect internal whistleblowers and conduct investigations into reported misconduct.<sup>1112</sup> There is a lack of clarity about how to implement internal procedures in listed companies. For example, companies may issue rules on internal disclosure with only minimum standards, which does not serve the regulatory purpose of protecting market integrity. The CMA does not publish any policy statement or guidelines giving preference to certain types of internal procedures, so listed companies can implement rules without serving the purpose.

In contrast, the FCA continuously publishes policy statements and information about whistleblowing to increase awareness and enhance trust in the system.<sup>1113</sup> This is a lesson learned from the 2008 financial crisis. Before the 2008 financial crisis the UK faced the same shortcomings as Kuwait in terms of lack of comprehensive whistleblowing policies in the ‘big five’ UK banks, namely Northern Rock, RBS, Lloyds, Barclays and HSBC.<sup>1114</sup> An analysis of those banks for the period before the 2008 crisis shows that some of them did not have whistleblowing policies while others only met minimum standards.<sup>1115</sup> Thus it is important to oblige listed companies to have comprehensive whistleblowing policies with adequate protection for whistleblowers and assurances that reported crimes will be investigated. The author of the analysis made three main recommendations for the FCA to adopt better internal whistleblowing policies. Those recommendations, detailed below, could now be taken up by the CMA to create a better whistleblowing regime.<sup>1116</sup>

‘First, financial organisations need to incorporate standardized whistle-blowing policies into their workplace and into employee’s contracts. This would ensure that employee’s

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<sup>1111</sup> The CML Executive Bylaws, Module Fifteen, Chapter Seven, Article 7-3

<sup>1112</sup> Alison Lui, above, (n 1003), 9.

<sup>1113</sup> FCA, ‘FCA Introduces New Rules on Whistleblowing’ dated 19 April 2016 available at <<  
<https://www.fca.org.uk/news/press-releases/fca-introduces-new-rules-whistleblowing>>> accessed 7  
 February 2020.

<sup>1114</sup> Alison Lui, above, (n 1003) 8.

<sup>1115</sup> Ibid.

<sup>1116</sup> *ibid.* 16-17.

legitimate concerns are taken seriously and give employees protection from wrongful dismissal if the policy is not followed. Secondly, the FCA should work with an independent professional regulatory body for bankers and develop a standardized Code of Conduct for banker. They should also be prepared to take enforcement action against rogue bankers. Thirdly, to ensure that there is Chief Risk Officers should be able to raise concerns with the regulator freely and openly. They should act together as ‘gatekeeper’. Chief Risk Officers will have a power of veto and sit on the board of directors and act as the chairman of Board Risk Committee. Institutional investors should work with the regulator to ensure that wider stakeholders’ interests are taken into account and actioned.’

Furthermore, the governance regulation does not oblige an employee to whistleblow a crime internally before reporting it to the external authority. It is good practice to facilitate internal reporting procedures for whistleblowers in listed companies, and authorities are also recommended to facilitate reporting to the parliamentary ombudsperson, which should have the power and jurisdiction to investigate whistleblowers’ concerns.<sup>1117</sup> Although it is good practice to provide more channels for employee whistleblowing, in Kuwait the National Assembly does not have the specialist expertise to investigate insider dealing in stock markets.

The CMA can use a risk-based approach to evaluate the procedures that companies adopt to report internal illegal activities, and distinguish between them based on the effectiveness of the internal whistleblowing regimes. Listed companies with a huge impact on stock markets should be categorised as high risk. This assessment helps the CMA and Nazaha to focus their limited resources on supervising the highest-risk listed companies. Looking at stock markets in terms of wrongdoers and their potential to commit crimes gives the supervisory authority a good picture of its capability to enforce Kuwait’s whistleblowing regime.

#### 4.2 Use of incentives to encourage reporting

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<sup>1117</sup> *ibid.* 8.

An efficient whistleblowing regime depends on adequate protection and sufficient reporting procedures to protect the market's integrity, but there are other elements that can help to increase effectiveness, like rewards and a good environment.

#### 4.2.1 Rewards

The 2008 financial crisis highlighted the limitations of financial regulators' knowledge about inside information,<sup>1118</sup> hence many jurisdictions reformed their whistleblowing regimes to encourage knowledgeable individuals to come forward to reveal crimes and misconduct. The US adopted the Dodd-Frank Act, which creates monetary incentives to whistleblowers who provide the competent authority with original information.<sup>1119</sup> An important element in an effective whistleblowing regime is a reward system to encourage people to reveal wrongdoing in their companies.<sup>1120</sup> Although incentives and rewards for reporting crimes are not fundamental measures in a good regime,<sup>1121</sup> it is important to encourage individuals to report by offering benefits. The UK and Kuwait do not have monetary incentives for whistleblowers. The US approach is a leading example of the adoption of a reward system to encourage individuals to whistleblow wrongdoing, and the US experience has persuaded other jurisdictions to adopt the same policy.<sup>1122</sup> Whistleblowers will be entitled to monetary reward if they provide original information in good faith to a competent authority.<sup>1123</sup> The reward is a percentage of the sanction, ranging between 10 per cent and 30 per cent of the collected amount.<sup>1124</sup> The US financial regulator made 18 awards to 23 whistleblowers, one of whom received \$30 million.<sup>1125</sup> It means there were successful cases based on whistleblowers reports. This indicates that people will be encouraged to whistleblow crime and misconduct if there are monetary reward available.

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<sup>1118</sup> Neil Schonert, 'A Fistful of Dollars: Bounty Hunting under the Dodd-Frank Act's Whistleblower Provisions' (2011) 36 Southern Illinois University Law Journal 159, 159.

<sup>1119</sup> *Ibid.*, 170

<sup>1120</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 18 March 2020.

<sup>1121</sup> *ibid.*

<sup>1122</sup> Neil Schonert, above (n 1118) 160.

<sup>1123</sup> *Ibid.*

<sup>1124</sup> *Ibid.* 171. The US Dodd-Frank Act

<sup>1125</sup> Mohammad Al-Mutairi, above, (n 24) 172.

Insider trading in stock markets may be worth millions, so offering financial rewards will encourage individuals to blow the whistle on their employers more often. There is no financial reward for whistleblowing in Kuwaiti stock markets, and it would be advisable to amend the law to include rewards to encourage people to report suspected crimes more often. If a person could get 1 per cent of the value of the insider trade as a reward for his/her act in revealing the crime, more people will be encouraged to blow the whistle on illegal trading. As an example, in 2013 the Kuwait Appeal Court gave an estimated value for insider dealing of 1.5 million Kuwait dinars (approximately £3,777.72),<sup>1126</sup> so if a 1 per cent reward system is implemented the whistleblowers will get at least 1000 Thousand dinars as reward for their reporting.

Individual motivations to report misconduct are varied. Some employees want revenge, while others are interested in a reward.<sup>1127</sup> Compensation is regulated by Article 43 of the Anti-Corruption Law, which states that Kuwait is under an obligation to compensate the whistleblower for material or other damages that he/she may sustain as a result of submission of his/her whistleblowing report of corruption. Compensation is a positive factor encouraging employees to blow the whistle on wrongdoing, and helps to recompense any financial damage the whistleblower might face after reporting the wrongdoing, or is at least an attempt to provide a remedy. Another factor motivating employees to report misconduct is Civil Service Law No. 15 of 1979, which instructs the employee to protect the dignity of his/her position in the company and conduct himself/herself properly. This indicates that protection of the public interest should be a responsibility shared between government and individuals. But regardless of the individual motivation to report misconduct, the superior authority or entity in charge must take the necessary steps to investigate the report.

There are no monetary incentives in the CML and its Executive Bylaws. It is important to encourage individuals to come forward and report insider trading, but requiring credible documentary evidence with documents while providing no incentive might leave the market without any reporting tool. This gap needs to be covered by the CML to motivate individuals to blow the whistle on insider trading.

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<sup>1126</sup> Kuwait Appeal Court, Case No. 15/2014 Criminal Division issued on 25/11/2014

<sup>1127</sup> Jonathan Macey, above, (n 995) 35.

The UK approach does not provide a financial reward either. The argument is that there is no link between a whistleblowing report and a financial reward to encourage individuals to report misconduct.<sup>1128</sup> The FCA and PRA explained that financial rewards might affect the whistleblowing system negatively in comparison to the US system for several reasons, of which the main ones are listed below.<sup>1129</sup>

- Incentives in the US only benefit the small number of people whose information leads directly to successful enforcement action resulting in the imposition of fines – they provide nothing for the vast majority of whistleblowers.
- There is no empirical evidence of incentives leading to an increase in the number or quality of disclosures made.
- The incentives system has generated significant legal fees for both whistleblowers and firms.
- There is a risk that financial incentives might lead to an increase in malicious reporting.
- There is a risk that some market participants might seek to entrap others in wrongful activity to enable them to blow the whistle and benefit financially.
- There may be conflicts of interest in court: if a whistleblower's disclosure leads to a criminal prosecution, the court could call into question the reliability of the evidence because the witness stands to gain financially.

These reasons might be valid in the UK situation, but a reward system is needed to change Kuwaiti culture to report crimes and protect market integrity. People should be rewarded for the stress of blowing the whistle on their employers.<sup>1130</sup> The system should not reward all whistleblowers, but only those who provide information that leads directly to preventing or detecting insider trading. The idea of allowing people to benefit from their cooperation in protecting the markets will change the culture and encourage more people to engage with the whistleblowing system. The CMA needs to change the

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<sup>1128</sup> FCA and PRA report about Financial Incentives for Whistleblowers dated July 2014 Available at <<  
<https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/financial-incentives-for-whistleblowers>>> accessed 18 March 2020.

<sup>1129</sup> Alexandra Webster, above, (n 999) 70.

<sup>1130</sup> This is one of the arguments to implement financial incentives in UK approach Alexandra Webster, above, (n 999) 66.



culture in Kuwaiti society to implement an effective whistleblowing regime, and providing financial rewards will help in this.

In terms of the importance of financial rewards, the UK has a more developed understanding of the whistleblowing system thanks to the FCA publishing public statements and raising awareness of the system.<sup>1131</sup> In Kuwait neither the CMA nor Nazaha puts any effort into increasing public awareness of whistleblowing, so including financial rewards might encourage people to take steps to combat insider trading if they benefit from the action. The UK is a more mature market and does not need financial rewards to encourage people to come forward, unlike Kuwaiti stock markets. It seems the CMA needs time to establish a strong culture and greater understanding of the importance of the whistleblower's role in protecting the public interest, and it is advisable to include financial rewards as part of this.

The interviewees confirmed that there is lack of public awareness about the whistleblowing system.

Participant No. 3 stated:

In insider dealing crimes people should be able to whistleblow the crime because there is a system and a procedure to achieve this trust, by involving people to protect the markets from insider dealing. But in reality, who has the interest to whistleblow insider dealing? Additionally, the CMA did not play their role by increasing knowledge and awareness or encourage people by offering a financial reward to whistleblow insider dealing.

#### 4.2.2 Environment

Availability of data on a sensitive issue like whistleblowing has been a problem. Social media have a huge effect on people's lives and decisions, so any misleading information in the media could be disastrous for stock markets. The CMA does not release any official statistics about whistleblowing reports in the public domain, so there is no record of the number of reports of insider trading. Even Nazaha does not publish any statement about financial crime or insider trading in its annual report. This research

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<sup>1131</sup> Alexandra Webster, above, (n 999) 68.

relied on publicly available information to present a general picture about the Kuwaiti whistleblowing regime in stock markets. In the UK the FCA and the PRA started publishing annual reports on the STOR disclosures they receive and their outcomes in autumn 2014.<sup>1132</sup> The FCA has a page on its website indicating the number of STORs it has received over the last year;<sup>1133</sup> it publishes the outcomes of cases and contacts the whistleblowers to thank them.<sup>1134</sup> Tracey McDermott, acting FCA chief executive, commented:

Whistle-blowers play an important role in exposing poor practice in firms and they have in the past few years contributed intelligence crucial to action taken against firms and individuals. It is in the interests of the industry and regulators alike that wrongdoing is identified and addressed promptly. For individuals to have the confidence to come forward, it is vital that firms have in place adequate policies on dealing with whistleblowers and that a senior manager takes responsibility for overseeing these policies.<sup>1135</sup>

The FCA highlights the importance of the whistleblowers' role in protecting the financial sector from wrongdoing, and enhances whistleblowers' trust and confidence that the authorities will take the necessary steps to prevent and detect wrongdoing. It is crucial to ensure that the industry and individuals are well informed about their part in protecting the markets.

Another important element is communication after whistleblowing: the competent authority must communicate with the whistleblower to ensure he/she suffers no harm in the workplace, and the FCA has improved its feedback system to help assess whistleblowing report outcomes.<sup>1136</sup> There are no such procedures in Kuwait: neither

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<sup>1132</sup> Point 18 of FCA and PRA report about Financial Incentives for Whistleblowers dated July 2014 Available at << <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/financial-incentives-for-whistleblowers>>> accessed 18 March 2020. also see The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020. Also see Alexandra Webster, above, n994, 71

<sup>1133</sup> The FCA website available at <<https://www.fca.org.uk/markets/suspicious-transaction-and-order-reports/number-stors-received-2018>> accessed 6 February 2020.

<sup>1134</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020.

<sup>1135</sup> FCA website available at << <https://www.fca.org.uk/news/press-releases/fca-introduces-new-rules-whistleblowing>>> accessed 6 February 2020.

<sup>1136</sup> The FCA report, 'How We Handle the Disclosures from Whistleblowers' dated February 2015 available at << <https://www.fca.org.uk/publication/corporate/how-we-handle-disclosures-from-whistleblowers.pdf>>> accessed 18 March 2020

the CMA nor Nazaha provides any kind of contact after a whistleblower reports an insider trading crime. There is no framework for connection to ensure whistleblower protection. It is suggested that a follow-up department should be created to communicate with whistleblowers and ensure they are protected.

#### 4.2.3 Hotlines

It is crucial to have good whistleblower reporting mechanisms to ensure an effective regime.<sup>1137</sup> There are weaknesses in the CMA system of receiving reports of insider trading, and there is no online channel or mechanism to blow the whistle on a listed company. The procedures for submitting a report must be easy and quick. Using new technology, like an online whistleblowing site, would facilitate an efficient reporting system.

The interviewees highlighted the weaknesses in whistleblowing procedures and confirmed that these need to be developed. Participant No. 2 stated:

We cannot conclude how people are aware of the whistleblowing process and mechanisms, but the whistleblowing reports are very few/rare. It is necessary to improve people's awareness about the whistleblowing system and how it works. The CMA must issue guidance and provide guidelines to whistleblow any illegal activities. The CMA must simplify the whistleblowing process by allowing the submission of their whistleblowing reports online.

Participant No. 4 insisted that new systems to receive whistleblowing reports of insider trading should be adopted, such as a government webpage:

The government must create online channels like a government window to whistleblow any crime in Kuwait. New mechanisms must be introduced in Kuwait to change the culture about whistleblowing.

This is unlike the UK approach, where the FCA uses every possible channel to facilitate whistleblowing reports. It provides phone numbers and email addresses to report any wrongdoing.<sup>1138</sup> This ensures that a whistleblower feels free to select the most appropriate mechanism to report the crime.

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<sup>1137</sup> OECD 'Protection of Whistle-blower' May 2011 available at <<https://www.oecd.org/g20/topics/anti-corruption/48972967.pdf>> accessed 6 February 2020.

<sup>1138</sup> The FCA website, Whistleblowing available at << <https://www.fca.org.uk/firms/whistleblowing>>> accessed 18 March 2020.

## 5. Conclusion

An effective whistleblowing regime deters insider trading; facilitates the reporting of crimes without fear of legal consequences; helps identify any attempted insider trading early on, and thereby prevents potentially grave disasters; and reduces the risk of potentially damaging external reports, including to regulators or the media. The whistleblowing regime is based on the fundamental principle that protection of the public interest is a responsibility shared between government and individuals. It provides a channel for individuals to play their role in protecting the public interest by blowing the whistle on any insider trading in stock markets. But a whistleblowing regime cannot be effectively implemented without raising awareness and strengthening communication and training. The CMA needs to change Kuwaiti culture, provide adequate protection to whistleblowers, establish clear guidelines regarding the purpose and principles of whistleblowing, and publicise the benefits of having a strong whistleblowing regime. It should issue a paper regarding the introduction of a whistleblowing culture in stock markets, similar to the UK approach.<sup>1139</sup>

This analysis shows that the CML gives a narrow and restrictive legal framework for whistleblowing insider trading in stock markets. There are strict conditions and requirements that are almost impossible to fulfil, especially when they involve providing credible evidence of insider dealing. Insider trading is a highly technical fraud in stock markets, and there cannot be such strict restrictions in reporting it. Furthermore, the Anti-Corruption Law does not include financial crimes as corruption crime, and this limits the Kuwaiti whistleblowing system and produces an insufficient regime in stock markets. It is suggested that the Anti-Corruption Law is reformed to include financial crimes as corruption crime. Another suggestion is to establish a joint committee to coordinate and exchange information about reported financial crime and raise public awareness about the whistleblowing regime. The move towards risk-based supervision requires the CMA and Nazaha to work together to increase awareness of the system and to cooperate fully in investigations.

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<sup>1139</sup> The FSA introduced a paper to increase the industry awareness about the whistleblowing system-FSA chief calls on traders to 'clean up City' The Guardian, 25/1/01

Furthermore, the CMA has not published any guidelines or policies to encourage employees to blow the whistle on insider trading. There is a lack of awareness and understanding of the whistleblowing regime in stock markets, which affects the effectiveness of the system in Kuwait. Thus it is suggested that a programme should be established by Nazaha and the CMA to train their staff and listed companies' employees about whistleblowing.

Protection of the whistleblower is the main weakness in the Kuwaiti regime. There is no provision for a new identity or effective legal, civil or criminal protection. Indeed, the whistleblower may be punished with a fine or imprisonment if he/she fails to prove his/her allegation or fails to show that he/she acted in good faith in reporting misconduct. This has to be changed immediately to guarantee protection for whistleblowers, especially since insider trading is a complex crime that must be investigated and proven by experts. It is necessary to reform the current protection programme to give a whistleblower more realistic protection, including a new identity in another country.

This chapter discusses ways to encourage individuals to blow the whistle on wrongdoing. It argues that financial reward is a positive practice to encourage employees to report misconduct in their organisations. It also helps employees to be compensated for any potential losses. Another factor is creating a good environment to encourage individuals to report by publishing whistleblowing outcomes and providing hotlines for reporting.

Furthermore, there is an absence of communication after crimes are reported. It is essential to create a channel of communication after reports are submitted to ensure that the whistleblower is safe and to obtain more information about the crime. Whistleblowing cases are very sensitive crimes, and whistleblowers must be handled carefully. Finally, there is a lack of published whistleblowing reports, and public data and information are important to enhance trust and confidence in the stock markets. Publication of whistleblowing outcomes in the CMA's annual report is important to change the culture of Kuwaiti society. The clear message is that existing whistleblowing programmes and protection available for individuals need to be upgraded.

## **Chapter 9: Conclusion**

This thesis examines the effectiveness of insider trading regulations using a risk-based approach to analyse the data. It explores the implementation and application of Kuwait Capital Markets Law (CML) No. 7 of 2010, which regulates the most important aspects of the country's economy, including financial services and stock markets. This thesis aims to present a risk-based approach to regulation analysis and identify any shortcomings in Kuwaiti regulations in place to govern financial services and insider trading in stock markets. In addition, it analyses laws and regulations in terms of their compliance with International Organization of Securities Commissions (IOSCO) standards before drawing comparisons with the UK approach to reveal deficiencies in the Kuwaiti approach. This thesis includes a discussion of the Capital Markets Authority (CMA) in terms of its independence from influence, accountability for its actions, and its ability to effectively regulate, deter, and discover insider trading. It assesses the disclosure regime, the legal framework for regulating and punishing insider trading, and the whistle-blowing system's efficacy as method of discovering criminal activity. Finally, as its primary contribution, it serves as a foundation for further discussion of the challenges that the CMA faces in introducing a risk-based approach to regulation.

### **1. Outline**

Chapter 1 introduces the study and highlights the research context and key arguments. It provides a brief history of the CML and explains the main research question, objectives, methodology, and limitations of the study. It includes a literature review covering prior studies on the subject. It summarizes the main contributions of this study and outlines the research structure.

Chapter 2 explains why risk-based and forward-looking systems are the best approaches to judging the efficacy of regulations. It discusses the preconditions that must be in place for these two systems to be applied properly. An investigation of the forward-looking approach's conditions and requirements shows that the CMA does not have the capacity to adopt and apply this approach based on its structure and level of expertise. A risk-based approach is more appropriate for Kuwait, but its adoption also has drawbacks. The chapter notes two shortcomings of risk-based regimes affect Kuwaiti insider trading regulation: there is no published policy, and there is no organisational culture with which to implement a risk-based

regime. Furthermore, shifting to a forward-looking, judgement-based approach brings its own challenges. Obstacles arise in several different areas: There are constitutional issues over maintaining the accountability of regulators, and there are practical issues such the different skills required of supervisors, compliance staff, and enforcers. New strategies centred on dialogue are needed to build relationships between the CMA and regulated firms; however, engaging in such strategic and constructive dialogue places significant demands on the regulatory culture and the capacities of all those involved in financial service and stock market regulation. This includes both regulated firms and the CMA. The necessary capabilities do not currently exist within the Kuwaiti regime in terms of qualified supervisors and channels for dialogue with regulated firms. However, the CMA has taken some steps via internal policy toward adopting a risk-based approach. In this chapter, the conclusion that the risk-based approach is suitable for effective supervision and enforcement of financial regulations in Kuwait is explained, and concerns about the fact that Kuwaiti officials and experts interviewed as part of this research are unfamiliar with the philosophy behind the risk-based approach to regulation and the way it interacts with other regulation strategies, such as judgement-based and meta-regulation approaches, are allayed. The remaining chapters investigate the risk-based approach to regulation and highlight the deficiencies in the Kuwaiti system, suggesting recommendations for its application.

Chapter 3 provides an overview of the Kuwaiti legal system in terms of oversight and the structure of supervisory authorities overseeing the financial sector. It explains the regulatory framework currently applied to the Kuwaiti stock markets, and how it works to supervise the markets and enforce the law. This chapter also covers the democratic oversight system in Kuwait, which sets up the legal basis for the independence and accountability of the CMA. In Kuwait, public authorities are under the umbrella of the Council of Ministers' executive branch, giving the National Assembly the ability to hold the incumbent minister of Ministry of Commerce and Industry (MOCI) to account for misuses of power or incorrect decisions made by the CMA. The chapter explains the shift of supervisory responsibility for the non-banking sector, from the Central Bank of Kuwait (CBK) to the CMA, and the coordination required to fill regulatory gaps and avoid the duplication of procedures between authorities. The responsibilities between the two authorities needed to be organised and a clear legal framework separating them set out to ensure that supervision of the financial markets was placed securely under the auspice of CMA. In addition, the involvement of the MOCI in the creation of

companies and issuance of licences required more coordination and cooperation with the CMA to establish unified rules. The CMA's relationships with the CBK and the MOCI were outlined in MoUs that contain the legal framework for cooperation between these authorities. This chapter illustrates the challenges in establishing effective coordination between these authorities and the resulting weaknesses in terms of regulatory application. A lack of rules obliging one authority to inform or respond to any requirements of or concerns expressed by another authority, and the absence of deadlines for replying and addressing another authority negatively affects coordination efforts between them. The main purpose of this coordination is to exchange information and ensure that regulators are fully aware of any important information affect their objectives, priorities, and resource allocation. This provides an opportunity to explore a new risk-based approach to regulation; the structure of the current system and its lack of coordination highlights loopholes that could lead to unpredicted financial consequences.

Chapter 4 analyses the CMA architecture in terms of its position as an independent yet accountable authority. This chapter first confirms that the CMA is a single, unified regulatory body with responsibility for providing oversight of the stock markets and financial services. The CML sets forth objectives but does not explain the mechanisms to be used to attain these objectives, and there is an absence of publicly published policies to clarify the CMA's strategy. Another important point highlighted in this chapter is that the annual report is general and descriptive, and it does not provide sufficient detail about the achieved objectives. This chapter goes on to demonstrate that the boundaries between administrative independence and governmental accountability are not clear; while the law grants the CMA independence, it is not, in practice, operationally independent and free from external political or commercial interference. The minister of MOCI nominates commissioners,<sup>1140</sup> proposes the commissioners' remuneration,<sup>1141</sup> and approves and supports the CMA budget. As a result, the CMA Board of Commissioners, and in particular the chair, is bound to the government and subject to influence from various agendas. The chair and other board members have various motives for accepting and maintain their posts: Social standing and the advantages gained from networking are primary, but they also gain satisfaction from contact with the minister who

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<sup>1140</sup> CML, Article 7.

<sup>1141</sup> CML, Article 11.



supervises the work of the authority.<sup>1142</sup> The chapter moves on to explain that the ability of the CMA to hold commissioners accountable for their decisions and actions should be reformed immediately as there is no mechanism in place to impose accountability on individual commissioners or the CMA as a whole. The Code of Conduct does not provide the necessary tools and power to question the CMA about its decisions, and any breach of the Code of Conduct cannot be punished if the CMA Board chooses not to mete out punishment. Finally, the legal framework used by the CMA to regulate the financial sector and stock markets does not employ best practices. This chapter uncovers the need for the CMA to improve its recruitment processes to avoid *wasta*.<sup>1143</sup> Training is needed to protect the CMA from corruption and undue influence that may arise out of its weakly structured autonomy. Finally, the lack of adequate staff training in CMA programmes has a significant impact on the application of the risk-based approach because this approach relies on the staff's capacity to assess risk and then set priorities accordingly. Without qualified, well-trained human resources, any application of a risk-based approach will be faulty, and the failure to apply a risk-based approach in the prioritisation of the CMA's objectives represents a serious oversight.

Chapter 5 investigates the CMA's powers and the tools used to enforce financial regulations. The chapter's analysis reveals that there is a positive development on this front: The CMA is gathering data on the powers and tools that will give it a sufficient legal structure for collecting information. This chapter also explores the CMA's broad powers to collect information, including the judicial power to inspect and investigate listed companies, before moving on to another important development in June 2019 when the CMA adopted (without any public statement) the risk-based approach as a policy to manage its on- and off-site inspection visits. However, the risk-based approach requires a proper understanding between regulators and the regulated firms; the CMA's new policy is still unclear and unpublished. Despite recent developments, the CMA's enforcement powers remain insufficient in terms of supporting the risk-based approach for five reasons: (1) The CMA still relies on deterrence more than a compliance approach, resulting in greater demands in terms of human resources, money, and time; (2) There is a maximum financial penalty for non-compliance which does not provide sufficient deterrence; (3) There is insufficient regulation of the publication of violations on the

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<sup>1142</sup> CML, Article 2.

<sup>1143</sup> An Arabic word that refers to using one's connections and/or influence to get things done, including government transactions such as getting hired for, or promoted in, a job.

CMA website which infringes on the privacy of non-compliant individuals and firms; (4) Collected penalties are added to the CMA's budget which creates conflicts of interest and damages the perception of the CMA's ethical position; and (5) There is no settlement agreement system to settle any violation of the CML with the CMA which results in inconsistent practices concerning such violations. The chapter demonstrates that the current CMA enforcement powers and tools do not represent best practices nor incorporate IOSCO standards and objectives. At the core of the risk-based approach to regulation is the ability to gather data and analyse it to correctly set priorities and allocate resources. Enforcement powers help to correct misbehaviour and violations and ensure a market remains safe for investors; without proper enforcement powers and tools to correct regulated firms' behaviour in the stock market, the market will be unprotected and vulnerable to abuse.

Chapter 6 examines efforts to tackle insider trading by requiring listed companies to disclose material information and thereby ensure investors have equal access to inside information. The chapter begins by explaining that the CML and CMA fail to provide listed companies with clarification and guidance on what constitutes material information. The prudent investor test is an obstacle for listed companies who want to properly disclose information, and there is no public policy statement about disclosure obligations that would clarify the situation. The next section points out an important drawback in the current Kuwaiti disclosure regime: the lack of a waiting period after inside information is disclosed. This loophole allows an insider to position themselves to use inside information immediately after its announcement but far ahead of others without facing legal consequences. After that, it goes on to discuss the regulatory gap that prevents the regulation of rumours and news, especially on social media. The existing regulations are too general in nature and do not cover the most modern news providers such as Twitter and Facebook. Another weakness is that the procedures and methods for receiving a disclosure are complex and contain unnecessary and wasteful duplications. The CMA has not yet fully implemented the XBRL software system, which is designed to receive disclosures without duplication and correctly analyse them to alert the regulators to the highest-risk firms. The slow implementation of the XBRL system damages investor trust and confidence in a strong disclosure regime. The chapter also discusses expert interviews which indicate that the quality of disclosures is weak and does not reflect a company's performance. This chapter shows that listed companies need only announce a minimum amount of information without offering any clarification or direction concerning the financial consequences of the information

on a particular stock. The final section discusses the implementation of good practices such as the 2015 CML amendments obliging companies to provide insider lists covering all individuals who have access to material/inside information. While a good step, there remains room for improvement because there is uncertainty about what or who constitutes the third type of insider identified as ‘others,’ and there is no guidance as to how listed companies would recognise someone in this category. Regardless of the shortcoming, enforcing the insider list is a promising development in stock market oversight. Correct information assists the risk-based approach in assessing risk and setting priorities, and without proper disclosures, the application of this approach will always be poor and may damage the markets.

Chapter 7 clarifies the legal framework of insider trading in stock markets and reveals the deficiencies in the Kuwaiti legal system. Identification of risk is the first step in formulating risk-based regulation, and unclear definitions negatively affect the proper application of the approach. This chapter outlines the weaknesses in insider trading regulation by first discussing the CML and its Executive Bylaws failure to provide a comprehensive definition of what constitutes the crime of insider trading. No distinctions are made between selling and purchasing or between making a profit and avoiding a loss. They fail to establish the legal responsibilities of listed companies’ insiders. This is followed by an examination of the insufficient definitions of inside information and insiders, which are the main weaknesses of the regulations. Currently, the definition of inside information is linked to the disclosure of information without ensuring public knowledge of the disclosure; this leaves room for insiders to exploit the gap and trade in the markets without any legal consequences. The chapter then moves on to show that the definition of insider is too broad and vague. After the 2015 amendments, the law includes a third type of insider described as ‘others,’ but without offering further explanation or illustration. This makes it hard for listed companies attempting to comply in good faith to create insider lists for the CMA and Boursa. The next discussion looks at another important shortcoming in the insider trading regulations: the absence of a distinction between insiders in terms of their responsibilities and punishments. The same criminal penalties apply to primary and secondary insiders, without taking into consideration their seniority within the company. Neither do the regulations recognise ‘inaction’ as a type of prohibited activity, and, contrary to custom in Kuwait, the listed prohibited activities do not cover all the possible scenarios. In addition, the iterated prohibited activities do not cover territoriality to prohibit and deter insider trading from occurring both inside and outside

Kuwait, and the CML should take into consideration any non-Kuwait activity by a listed company. All of the weaknesses detailed in this chapter affect the proper application of a risk-based approach to regulation because unidentified risks affect the CMA's responses in terms of allocating its resources, and loopholes need to be closed to have effective insider trading regulations.

Chapter 8 explores the whistle-blowing regime in Kuwait in terms of the stock markets and the program's effectiveness in deterring and uncovering insider trading. The chapter highlights the significant absence of widespread awareness of whistle-blowing and whistle-blower protection. By not providing an adequate regulatory environment, education, and support, the whistle-blowing structure fails to encourage people to act as whistle-blowers and come forward to report insider trading. In the current structure, all whistle-blowing reports in Kuwait go to the CMA—although the Anti-Corruption Authority (Nazaha) is allowed to receive reports in exceptional cases when insider trading relates to money laundering. The insufficient resources and onerous requirements under which individuals must file a whistle-blowing report hinder reporting. For example, one requirement that the whistle-blower must provide credible evidence of insider trading; this is difficult in practice because this is a complex and often undocumented crime which is difficult to prove in the absence of a paper trail or other hard evidence. Another hindrance is the inadequate protection given to whistle-blowers; the CMA can require compensation or penalties for incorrect information, and there is even a mechanism by which a reported insider may seek compensation, which is the very opposite of using whistle-blowing as a channel to allow people to provide valuable information to regulators without facing legal consequences or damaging their positions. The chapter also shows that there is often no CMA follow-up on whistle-blower information taking the necessary steps to uncover the crime. Neither does the whistle-blowing scheme offer any encouragement in the form of financial incentives for reporting suspicion transactions. Kuwait is different from the UK in terms of public awareness of the dangers of insider trading and the damage insider trading does to the market's integrity. Kuwait must work harder to encourage people to report this crime, so offering financial incentives, as is done in the US, is one mechanism that can be employed to help to change the culture. The situation with the structure of the whistle-blowing program has negatively affected the risk-based approach to regulation, so the CMA must reform the current regime to establish adequate whistle-blower protections, reasonable whistle-blowing requirements, and appealing incentives.

## **2. Thesis findings**

All the information discussed in these eight chapters shows that the CMA does not have effective regulation to tackle and prevent insider trading in stock markets, and this answers the key research question. The CMA's present ability to prevent insider trading in the stock market is inadequate to the task. Adopting risk-based approach to regulations is necessary for the CMA's to achieve its objectives and develop the current approach to supervision and enforcement into something more effective. The above analyses show that a risk-based approach to regulation is the best option to upgrade the current regulatory scheme. It also shows that the CMA cannot at this time adopt a forward-looking judgement approach due to its lack of sufficient experience and an appropriate structure. The CMA's best practice would be to acknowledge its current weaknesses, as highlighted during the 2008 global financial crisis, and employ the risk-based approach to addressing insider trading. It is important that the new approach provide effective regulation to deter, detect, and punish insider trading within the stock markets to avoid another financial crisis. A new governance policy is needed which provides the CMA with a clear plan to focus its limited resources on the areas of highest risk. In fact, the application of risk-based approach to regulation is part of a comprehensive strategy to protect the public interest by identifying risks and allocating the CMA's resources to protect the markets from individuals and listed companies most likely to engage in inside trading. This thesis highlights the need for a critical and contextual approach to govern risk which takes into consideration the existing legal, cultural, and experiential limitations on institutions and their practices. The risk concepts that are introduced in this thesis and applied to insider trading are also applicable to legal culture. When assessing the competence of public administration, limiting discretion, and holding decision-makers to account, risk governance concepts must be viewed in the context of the pre-existing constitutional and institutional frameworks.

The other major factor involved in moving towards the risk-based approach requires an increase in public awareness. The philosophy underlying the risk-based approach should be clear to regulators and regulated firms, and key players in the financial industry must understand the application of the approach as it is used to clarify the CMA's decisions and define its responsibilities in terms of protecting the markets. The new approach should help regulated firms to mitigate their insider trading risks according to their own assessments and priorities, allowing the regulators to limit their necessary interventions. Communication with

the industry is essential in the development and improvement of this approach, so the CMA must establish a centre to disseminate information about financial regulation policy reforms and changes.

Regulators will always have limited resources and risk-based methodology allows them to decide how to most effectively allocate those resources. The CMA's independence and freedom from external or political influences on its decisions must remain intact. In addition, it adds a layer of accountability by requiring the CMA members to clearly explain their decisions and justify their choices. The above analyses show that the CMA is not fully independent; it is still attached to the government and subject to governmental influence in all its decisions and actions. Moving forward, the CMA must become more independent when supervising stock market activities and enforcing the law. Currently, it is attached to the government through its incumbent minister in the MOCI and the Council of Ministers. The appointment process for the CMA Board of Commissioners must be changed so that nominations come from the private sector or commissioners are seated as the result of an election. The process must further stipulate certain educational and training standards for candidates to ensure only qualified commissioners are seated.

Remuneration for commissioners must be determined internally by the current CMA Board of Commissioners to maintain the board's independence. This situation is similar to that found in the Kuwait National Assembly, which is responsible for setting its own remuneration without interference from the government to reduce the potential for undue influence. The CMA's budget raises additional concerns about its independence and sources of unwarranted influence; at a minimum, these concerns may be addressed by refraining from making any administrative decisions during the budget approval process in the National Assembly. For example, if an MP wants to recruit someone for the CMA or ask for a promotion for any employee at the CMA, this decision would be suspended until after the CMA's budget is approved. An even better solution would be to allocate a separate funding source for the CMA to safeguard its independent position. An independent CMA is able to press charges against those who commit inside trading. If it may be alleged in any case that the CMA was influenced by a powerful political or private party to not investigate, call individuals to account for their behaviour, and press charges, it affects the public perception of market integrity and discourages market investors.

The interviews conducted in this study revealed that the government and parliament may change the structure of the CMA's Board of Commissioners to influence the CMA's decisions. This is a barrier to providing decent supervision and enforcement within the financial sector. The most dangerous card the government and the National Assembly have to play is their ability to change the structure of the CMA's Board of Commissioners from five members to one director, or to alter the CMA's responsibilities or limit its authority. Precautions need to be taken in advance to prevent this type of intervention before it occurs. Rules should be promulgated that restrict opportunities for change and apply conditions that must be satisfied prior to changes in the CMA structure. For example, any new law related to the CMA Board of Commissioners' structure should not be applied to the current board. Such a move would help limit external influences on any serious decisions that the CMA may be preparing to make.

At the same time, the accountability rules for the CMA Board of Commissioners must be redrafted to ensure that the framework is complete and appropriate. Currently, there is no adequate legal framework to hold members of the CMA Board to account. The Code of Conduct does not provide the necessary tools and powers to question the CMA about its decisions. This is problematic, and it does nothing to promote investor faith in the market's integrity. The Code of Conduct must be re-examined to set new rules which oblige the CMA Board of Commissioners to hold all commissioners to account for any misbehaviour, manifest lapse in judgement, or breach of duty. These rules must be well-structured, clear, and included in regular public statements to ensure their consistent application. The responsibilities of the CMA Board of Commissioners should be described by providing concrete examples and explanations of the scope of their roles as regulators. The Code of Conduct should also set forth the procedures for determining whether and when a commissioner is unqualified to act. In order to ensure an unbiased committee, it would be useful to establish a judiciary committee to investigate alleged violations committed by commissioners. The accountability of the CMA is important; if, as the result of external influence, the CMA's commissioners neglect their duties or fail to press charges against any individuals or listed companies who are shown to have committed the crime of insider trading, there must be visible consequences for those commissioners. This is a cornerstone principle that must be satisfied in order to have effective insider trading regulations in stock markets, and it is the main reason to develop better rules to protect the markets. In exchange for independence and autonomy, when regulations are not

applied because of improper external influences, there must be a mechanism to hold the CMA to account.

Another concern to be addressed is communication between the supervisory authorities overseeing the stock markets. The approaches to communication must be rearranged to avoid duplication and misrepresentation, especially when dealing with insider trading. The current failure by authorities to share information in a timely manner affects the application of a risk-based approach. Information is of tremendous importance when analysing the risks; without adopting proper procedures, the risk-based approach cannot be applied correctly. Insider trading is crime based on leaks of material information which has impact on stock markets. If criminals are sharing information as part of their offense, it is no less important that the sharing of information between the supervisory authorities is at least as thorough, efficient, and sophisticated as those they are attempting to monitor and deter. There are three levels of supervisory authority in Kuwait, and each level must have the appropriate tools and channels to exchange and share information with the others. In particular, the coordination between the CMA, the CBK, and the MOCI must be redesigned to clearly and overtly oblige each authority to share information with the other, particularly if it relates to insider trading. The CMA and the Boursa must establish a joint committee to exchange information until the XRBL system is fully implemented, and departments within the CMA must have fast, convenient, and adequate channels through which to share information. A specialist division similar to the proposed Risk-Based Supervision and Enforcement Department in the CMA should be created to implement the risk-based approach to inter- and intra-agency communication and ensure coordination between the trading, disclosure, and enforcement departments within the CMA.

In terms of the CMA's ability to uncover crimes and violations, it seems that it already has sufficient powers and tools (especially with the unusual grant of judicial power) to investigate alleged crimes and gather information. The real issue is the lack of adequate mechanisms to analyse the collected data and the unqualified staff who are present another obstacle to correct data analysis. Adopting a risk-based approach as policy will help the CMA to focus on the listed companies at highest risk who may commit insider trading based on a formal, data-based risk assessment. This strategy allocates the CMA's enforcement powers and tools to uncover crimes. Recently, the CMA adopted a risk-based approach as policy to develop a plan to inspect



the listed companies, but this policy is not published, and no public statement has been issued about the new risk-based approach.

Moreover, financial regulation enforcement is critical to protecting the markets from insider trading, other misbehaviour, and non-compliant firms. The CMA must adopt a new mechanism to analyse the available data and establish risks. For example, and most importantly, the CMA should amend its current enforcement powers in such a manner as to shift from a deterrence approach to a compliance approach. To this end, it is crucial to set compliance rules and encourage firms to comply by establishing discount and reward incentives for compliant firms. The rules should cover every aspect of the financial markets, and enforcement options should include the imposition of unlimited financial penalties to deter wilful non-compliance that arises out of a calculation demonstrating that the benefit of misbehaviour will exceed the maximum possible penalty. List companies who fail to timely and correctly disclose material information must be subject to fines substantial enough to make non-compliance unprofitable. Another important element to have effective insider trading regulations is clear framework that allows the CMA to settle with individuals and firms the consequences for transgressions. The CMA must issue new rules regarding settlement agreements outlining clear procedures to ensure all companies and individuals are aware of the CMA's process for negotiated or mediated resolutions. Settlement agreement power is a tool, and in the CMA's hands, it must be used according to clear rules to ensure fairness and justice.

Obliging listed companies and specified individuals to timely disclose material information affecting the stock markets is important mechanism for deterring insider trading. Precautionary procedures are in place to control any leaks of information, so the listed companies must disclose material information to the public and the CMA. Disclosure obligations must be sufficient to close regulatory gaps and protect markets from insider trading. As the above analyses show, the current disclosure regime which merely obliges listed companies to publish material information is insufficient. There is a lack of clarity in the definition of material information, and the description of disclosure is unworkably poor. Using the prudent investor test and linking it with material information makes the disclosure obligation unclear and attenuated. This must be changed, and following the UK approach which employs a 'reasonable investor' test appears to be a suitable solution.

Another important factor to prevent insider trading is to impose a waiting period after disclosed material information is disseminated in markets and to the CMA. Disclosure rules must be redrafted to include comprehensive definitions for terms and obligations. There should be a reasonable period of delay after the disclosure of material information, and to deter insider trading, the insiders must be forbidden from trading in stock markets during this waiting period.

The list of insider individuals must also be clear and sufficient. Listed companies must be obliged to disclose all individuals who have access to material information, and the nature of the 'others' type of insider should better defined and applicable in practice. The CMA must set new rules to address social media platforms. The new development of using social media platforms to spread rumours and news has had significant impact on stock markets. Therefore, the CMA must issue new rules to establish legal consequences for rumour mongers and news providers who aim to affect the stock markets with their communications. And, as the disclosure obligation encompasses even rumours and news, rumours and news transmitted via social media should be regulated; this includes the establishment of legal responsibility for a social media participants and the ability to charge social media providers, including those who operate in different jurisdictions. Finally, the CMA should promptly finish implementing the XBRL system to avoid any duplication of disclosure and waste of resources.

The key question of this thesis is the effectiveness of the insider trading regulations to prevent and address insider trading in stock markets by holding the insider trader to account via schemes based in criminal law or civil law. At this time, the CMA only uses a criminal regime to punish insiders, with no recognition of the benefits of the civil regime used in the UK approach. The analyses show that the legal framework limited to criminal law to establish insider responsibility is insufficient. There is no adequate definition of either the crime itself nor inside information.

The regulations concerning insider trading must be thoroughly reformed as the current framework has loopholes that stymie the prevention of insider trading. The insider trading framework should be clarified and explained, and a clear and thorough definition of each element of the crime must be provided with examples. The definition of inside information should be precise and clear enough to ensure its even application. The key to insider trading is the identification of the insider, so that definition must include clear explanations regarding the

‘others’ type of insider. Prohibited activities should be expanded to include encouragement and any other type of action that might aid the crime; in other words, the list of activities should be sufficiently detailed but broad enough to cover all situations. Furthermore, the scope of the prohibited activities must be extended to include insiders operating outside Kuwait.

Finally, in order to have effective insider trading regulations to prevent and address the crime, the whistle-blowing system is an important tool for discovering crimes or potential crimes. The current whistle-blowing system is unenforceable due the lack of legal protection and encouragement for whistle-blowers and the strict requirements requiring the production of credible evidence of insider trading. As it sits today, the whistle-blowing regime is worthless, and it does not give any substantial assistance to the CMA in terms of detecting and uncovering insider trading in the stock markets. To fix this, there should be no conditions forcing a whistle-blower to provide credible proof of a crime: The CMA must be responsible for investigating whistle-blower information and generating the necessary evidence. Most importantly, whistle-blowers must be protected and be allowed to remain anonymous to prevent any legal blowback or difficulties for themselves or their families. To change the culture and increase reporting, the CMA must include financial rewards as incentives for whistle-blowers. Finally, the CMA does not release policy statements or consultation papers regarding its policies on regulating insider trading, and it needs to publish its policies to encourage potential whistle-blowers to step forward.

The thesis conclusion shows clearly that there is a need to strengthen risk identification and management capacities, intensify regulations, move to more intrusive supervision, and deploy enforcement powers more assertively. To this end, establishing a skilled and qualified body of staff at the CMA is imperative. The trickle-down effect caused by the lack of understanding of financial regulations affects every aspect of the economy. The CMA staff and regulated firms’ employees must be made aware of the risk-based approach and its application. Furthermore, to shift the CMA’s limited resources away from one department to other high-risk areas requires thorough organisational reform. The CMA’s staff must have appropriate technical skills and qualifications with which to assess risks in the markets. An information system must be developed to identify the highest risks so that resources can be delegated efficiently and deployed properly. The existing staff must be trained and prepared to implement the risk-based approach.

### 3. Recommendations

To implement the risk-based approach to regulate insider trading in Kuwait, the CMA must tailor its regulatory rules to fit the circumstances of the markets. As Julia Black stated, '[A] Risk-based approach to regulation requires supervisory skills, an increased depth of experience, and an increase in resources.'<sup>1144</sup>

A lack of understanding of the approach can lead to system failure, poor design, and inappropriate implementation. This thesis provides the following five takeaway considerations for implementing a risk-based approach to tackling and preventing insider trading in Kuwaiti stock markets.

It worth mentioning that risk-based approaches to regulation can be applied in any subject in capital markets law involving manipulation. This approach helps to develop and improve the regulatory framework to provide better regulations, improve supervision, and evenly apply enforcement in any sector.

#### 3.1 Change in organisational structure

There are preconditions that the CMA must fulfil to apply the risk-based approach. It has been shown that rule-based regulations hinder the application of this approach due to their costly and time-consuming nature.<sup>1145</sup> Thus, the philosophy behind financial regulation in Kuwait must shift towards a principle-based approach to facilitate the application of the risk-based approach. The CMA's objectives must be clear, and the proper tools must exist or be created. The law is important in terms of determining the CMA's responsibility for protecting both investors and markets.

There are important abilities that a strong regulator must possess to apply the risk-based approach. In order to implement the risk-based approach correctly, the CMA must be both independent and accountable for their own decisions. As the above section explained, all the necessary rules and regulations must be reformed to adopt better regulations that ensure the

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<sup>1144</sup> Julia Black, above (n 80) 245.

<sup>1145</sup> IOSCO, 'Guidelines to Emerging Market Regulators Regarding Requirements for Minimum Entry and Continuous Risk-Based Supervision of Market Intermediaries', (2009) available at <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD314.pdf>> accessed 7 February 2020.

CMA is able to take necessary actions and make difficult decisions without any external influence.

### 3.2 Redrafting of regulations to prevent and address insider trading

In terms of the insider trading regulations to prevent and address the crime, the CMA must issue coherent regulations defining and explaining the crime of insider trading, starting with the definition of the crime and ending by explaining the whistle-blowing system. Each chapter of this thesis has explained in detail the framework for how to prevent and address insider trading. All the flaws identified herein must be reformed and regulatory or supervisory gaps must be closed to have an effective regulatory scheme. Organizing the rules into a set of unified regulations will make it easier for non-experts to understand, and certainty will contribute to deterrence.

### 3.3 Education and training

This is essential, and there must be an immediate move to establish a Capital Markets Law institution to teach and train the new financial regulations. The CMA staff and investors must have a proper education and training system to explain the law and educate them about its application. The CML clearly states that the CMA must establish a Capital Market Law institution, therefore, it is extremely important to implement this provision immediately. In addition to this new institution, both public and private universities in Kuwait must adopt capital markets law as a module in their courses for graduate student that aim to work in financial sector.

### 3.4 Industry awareness

The CMA must issue a public statement about their newly adopted policies and regulations. All key player in the markets must understand the CMA strategy for implementation of these policies. In fact, it must be reiterated in the CMA's annual reports, and unclear decisions or actions by the CMA must be open to discussion and clarification. Additionally, the CMA must change their methods in their workshops. Presenters must be able to explain the underlying policy of the CMA decisions and actions in the markets to educate and inform as a means of prevention and deterrence. Finally, the annual report must no longer be merely descriptive and contain more information about the ongoing litigation related to insider trading than the CMA's

other activities. Also, settlement agreements must be encouraged and disclosed in more detail in the annual report to allow the development of themes and promote discussion of the CMA policies and enforcement strategies.

## Appendix 1: Data Collection

The data collection method for this research involved the use of library resources along with fieldwork (interviews). Data were collected from primary and secondary sources, which is explained in the following.

### 1. Primary sources

This research uses text and fieldwork based sources. Fieldwork process and explanation was explained in the first chapter of this thesis. The following section covers text based source.

#### 1.1 Text based

The research is divided into two stages. The first stage mainly involved a desk-based approach. This part of the research is library oriented and doctrinal in nature. It consists of a traditional review of the textual data available as well as related reports found in various databases and libraries in the UK and Kuwait. In addition, IOSCO reports regarding the application of IOSCO objectives and principles in Kuwaiti financial markets were studied<sup>1146</sup> to identify key issues and concepts and the thesis's thematic framework.

To explain further, good governance regulations can help a national economy become more attractive to new investors wishing to participate in the domestic stock market.<sup>1147</sup> There is no formal governance structure dealing with cross-border supervision of global financial institutions, but there are laws and regulations proposed by international organisations that should be followed to apply best practices.<sup>1148</sup> The governance structure follows soft-law standards, which means that its non-binding laws and regulations are proposed by international bodies. It provides the best practices in the financial market but must be adopted as part of national law to be enforced.<sup>1149</sup> Soft-law standards must be effectively enforced to ensure that the market and investors are protected.<sup>1150</sup> It is worth mentioning that there is a connection

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<sup>1146</sup> The latest report on the application of IOSCO objectives and principles for securities regulation was in November 2004, which was before the new Capital Market Law No.7 of 2010 was issued, meaning that it is necessary to re-evaluate the status of the application of these objectives and principles in Kuwait.

<sup>1147</sup> OECD, 'The Need for Stronger Regulatory Governance' in *Regulatory Policy and Governance: Supporting Economic Growth and Serving the Public Interest* (OECD Publishing 2011) 74 <http://dx.doi.org/10.1787/9789264116573-7-en> accessed 6 February 2020.

<sup>1148</sup> Emiliós Avgouleas, 'Effective Governance of Global Financial Market: An Evolutionary Plan for Reform' (2013) 4 *Global Policy* (Supplement 1) 74, 77.

<sup>1149</sup> Chris Brummer, *Soft Law and the Global Financial System* (Cambridge University Press 2015) 3

<sup>1150</sup> Bashar AlGhanim, 'The Implication of Financial Regulation for Kuwait's Financial Sector' (8<sup>th</sup> Annual Conference of the EuroMed Academy of Business) 139.

between the protection of investors and a strong securities market.<sup>1151</sup> Therefore, to gain investors' trust and confidence, the supervisory authority in a market must have effective supervision tools and the ability to enforce the rules. The ability to implement the rules depends on the ability of regulators to carry out their role. To have a proper oversight process in place, it is necessary to apply international standards and good governance regulations in the economy and the legal system. IOSCO offers guidance and assistance for strengthening supervision in the financial sector and offers suggestions on how to apply best practices to avoid risk in the sector. IOSCO standards can help overcome weaknesses in the financial structure and improve securities regulation by adopting best practices.<sup>1152</sup>

## 2. Secondary sources

A wide range of materials were used, including but not limited to books, journal articles, newspapers, official websites and theses. An extensive review of the literature on financial regulations was conducted in English rather than Arabic. Arabic books were essential in establishing a clear understanding of the latest arguments and practical issues in the financial sector. The research also explored both Arabic and Western books and international organisations' reports to understand the best practices in financial regulation.

## Appendix 2: Data Analysis

Data analysis aims to identify themes by looking at patterns in collected data to address research questions and make conclusions about the examined issues.<sup>1153</sup> There are five stages of a qualitative data analysis framework.<sup>1154</sup> The process includes the following:

- Familiarisation
- Identifying a thematic framework
- Indexing
- Charting
- Mapping and interpretation

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<sup>1151</sup> Bernard Black above (n 12) 6.

<sup>1152</sup> IOSCO, 'Objectives and Principles of Securities Regulation', June 2010 <<https://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>> accessed 6 February 2020.

<sup>1153</sup> Moira Maguire and Brid Delahunt, 'Doing a Thematic Analysis: A Practical, Step-by-Step guide for Learning and Teaching Scholars' (2017) 9 AISHE-J: The All Ireland Journal of Teaching and Learning in Higher Education, 3351, 3352-3353.

<sup>1154</sup> Jane Ritchie and Liz Spencer, above (n 40) above 178- 190; also see Aashish Srivastava and S Bruce Thomson, above, (n 43) above 75.



Each stage mentioned above is part of the research process. It includes collecting and gathering related materials for review and analysis. The aim of the analytical approach is to describe and interpret what is already occurring in particular areas.<sup>1155</sup> There is some flexibility during analysis in terms of the order of the stages, but some must be in a logical order to create a thematic approach. Each stage is discussed in the following.

## **1. Familiarisation**

At this stage, the researcher reviewed the collected data to become familiar with the key issues addressed by the research. This included primary (legislation and judgments) and secondary (books and articles) sources in an effort to create a thematic framework for the research. According to Kamba, there are three phases of comparative law research.<sup>1156</sup> The first stage is the descriptive phase and involves a description of the legal system and its principles and concepts. In this phase, the problems and issues related to the research questions are explained. In this research, a descriptive style is used in each chapter to explain and clarify the problems and to suggest legal solutions by comparison with other systems, which, in our case, is the UK.

After highlighting the key issues, the researcher conducted interviews based on the research questions to discover insights and underlying policies and to validate the initial findings. The interview data were helpful to narrow the research scope to specific areas and to examine the initial findings. There is no doubt of the significant relationship between the problem/solution and its socio-cultural context.<sup>1157</sup> Therefore, the research investigated issues and solutions within the cultural context of Kuwait to reach solutions appropriate for the country by interviewing experts in the field to understand the public policy issues. Gutteridge points out the importance of culture context by stating, ‘The laws must be examined in the light of their political, social or economic purpose, and regard must be paid to their dynamic rather than to their static or doctrinal aspects’.<sup>1158</sup>

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<sup>1155</sup> Jane Ritchie and Liz Spencer, above (n 40) above, 176.

<sup>1156</sup> Walter Kamba, above (n 47) 511–512.

<sup>1157</sup> Walter Kamba, above (n 47) 513.

<sup>1158</sup> Gutteridge 174; also see Walter Kamba, above, (n 47) 514.

## **2. Identifying a framework**

After the familiarisation stage, the researcher recognised the key research issues and identified the themes from the collected data. The second stage is identification, as Kamba's identified which involves the clarification and classification of the key research issues.<sup>1159</sup> At this stage, the researcher dictated the themes and key issues of the study using analytical and logical thinking to identify the key issues in the financial sector and to ensure that all the research questions were being addressed and answered. The researcher used open coding that was developed and modified according to the data. In fact, pre-set codes do not provide the researcher flexibility to develop the work during the coding process.<sup>1160</sup>

## **3. Indexing**

The data were analysed, coded and categorised using a thematic approach. This involved the identification of all the collected data, either textual or that gathered from the interviews. The transcriptions of interviews with the seven experts were categorised along with the textual data. The process included making judgments about meaning and interpreting the data according to themes. Each theme must be separated to ensure a logical flow of the arguments. At this stage, the research framework became apparent.

## **4. Charting**

During this stage, data are 'lifted from their original context and rearranged according to the appropriate thematic reference'.<sup>1161</sup> In this research, the assessed data were divided into headings and subheadings according to the outcomes. The ordering and grouping of each argument were linked to the assessed data to suggest solutions for the key issues.

## **5. Mapping and interpretation**

This stage is the cornerstone of legal research and enables solutions to the key issues investigated in this research. The explanatory phases as Kamba referred to it as the third stage.<sup>1162</sup> It involves highlighting the deficiencies in Kuwait financial system. It is worth mentioning that the stages outlined above are not addressed separately in each chapter. Some

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<sup>1159</sup> Walter Kamba, above (n 47) 514.

<sup>1160</sup> Moira Maguire and Brid Delahunt, above (n 1153) 3355.

<sup>1161</sup> Jane Ritchie and Liz Spencer, above (n 40), 173, 182.

<sup>1162</sup> Peter De Cruz, 'Comparative Law, Functions and Methods' (2009) Max Planck Encyclopaedia of Public International Law, 1, 10.

chapters consist of two or three stages or phases that are used to explain the research questions and to offer solutions. Each chapter investigates legal problems and suggests better solutions by comparison with the UK system. Therefore, each chapter uses the three stages or phases of Kamba's methodology to conduct a comparative law analysis.

### Appendix 3 Fieldwork Questions. Semi-structured

#### Objectives

- To evaluate the CMA's understanding of risk-based approach to regulation
- The legal framework governing the CMA in terms of its independence and accountability
- The clarity of regulation and effectiveness in terms of preventing insider trading.
- Adequacy of human capital
- Regulator transparency to provide sufficient disclosure legal framework
- Adequate protection for whistle blower to whistle blow insider trading
- The legal framework for the enforcement and invoking of the CMA's supervisory powers

Chapter	Prove the problem	Questions
<b><u>Risk-based approach</u></b>	To prove the lack of understanding the risk-based approach to regulation.	<ol style="list-style-type: none"> <li>1. Does the risk-based approach help the CMA to oversight the regulated firms and prevent financial crisis?</li> <li>2. Do you think that if the CMA adopts priorities policy like FCA will help to provide effective supervision? How does the CMA set their priority?</li> </ol> <p><b><u>Problem with Inter-Industry communication:</u></b></p> <ol style="list-style-type: none"> <li>3. Does the CMA and CBK have adequate communication in term of sharing information –</li> <li>4. Does the CMA communicate with the industry to improve its supervision and enforcement? Is there a channel which allows listed company or firm to communicate with the CMA?</li> <li>5. Is the personal connection with the CMA is the basis for the dialog?</li> </ol> <p>-----</p> <ul style="list-style-type: none"> <li>- ماهي ابرز التغيرات في سوق الاوراق المالية بعد قانون هيئة اسواق المال 2010</li> <li>- ماهي السياسة العامة في تحديد اولويات في الرقابة على الشركات</li> <li>- هل يوجد الية لمراقبة الشركات الاكثر خطورة على الاقتصاد العامة للدولة وكيفية تحديدها بانها الاكثر خطورة</li> </ul>

		<p>- ما هي المنهجية المتبعة في الرقابة و الاشراف على السوق</p> <p>- هل المنهجية القائمة على المخاطر متبعة في الرقابة على الشركات</p>
<p><b><u>The structure the CMA in terms of its independency and accountability.</u></b></p>	<p>Accountability &amp; Independency Problem:</p> <p>To prove there is lack of independency and accountability.</p> <p>The CMA is attached to MCI in terms of its financial and decisionmaker.</p> <p>The CMA can be only account to the MCI. There is no really accountability from the parliament.</p>	<p>6. Does the Minister of Commerce and Industry have an influence over the CMA decision? Does the appointment of the CMA commissioners provide independency?</p> <p>7. Do you think the current practice to appoint the Board of Commissioner grant independency to the CMA?</p> <p>8. Would it be any different if the nomination of the commissioner by the public association such as The Chamber of Commerce and Industry, the Federation of Investment Companies, the Union of Banks of Kuwait and a number of related parties</p> <p>9. What do you think about the Governance Code for appointment of the public body like FCA?</p> <p>10. Does the MCI and Council Minister have influence on the CMA governing body because they determine their Remuneration</p> <p>11. Do you think it is better <b>if the CMA is supervised by the Parliament</b> not Ministry of Commerce and Industry to provide the CMA more independency from government influence?</p> <p>12. In the FCA approach, there is jointly appointed by the sec state and treasury can be applicably in the CMA?</p> <p>13. What about the FCA public annual meeting to discuss the latest report? There is no public discussion in kuwait to provide transparency to question the CMA's performance over the last year.?</p> <p>14. Is the accountably theme in Kuwait is effective. Does the CMA's accountability to the MCI is enough?</p> <p>15. Does the National Assembly have power to call the CMA to account? What about the referral of the governor of the CBK to prosecutor to investigate allegation of insider trading?</p> <p>16. Is the Code of Conduct enough basis of the CMA's responsibility? Does it provide clear guidance and determine the responsibility of the CMA.</p> <p>17. Do you think its conflict of interest that the financial penalties go to the <b>CMA budget</b> as it part of its financial resource, which might cause a conflict of interests because the authority might be tempted to increase the number of financial penalties? Unlike UK system, the penalties go to the Treasury after deducting the enforcement cost</p> <p>-----</p> <p>هل يوجد تأثيرات خارجية على قرارات الهيئة فيما يخص الرقابة على السوق ماهي الاجراءات المتبعة في تعيين المفوضين في هيئة اسواق المال هل الالية المتبعة توفر الاستقلالية عن الحكومة في اتخاذ القرارات هل الالية المتبعة في اختار المفوضين تأخذ في الاعتبار جمعيات النفع العام او غرفة التجار واتحاد المصارف هل التفرد من قبل الحكومة في تعيين المفوضين يوفر استقلالية للهيئة هل نتائج انتخابات مجلس الامة ياثّر في اختار المفوضين</p>

		<p>في حال حدوث نقص في الميزانية العامة للهيئة ماذا يمكن ان تفعل الهيئة لماذا الغرامات المالية تذهب الى ميزانية الهيئة وليس ميزانية العامة للدولة منعا لتضارب المصالح</p> <p>كيف يتم تحديد رواتب المفوضين</p> <p>ماذا عن سلطة الوزير في محاسبة المفوضين هل هي مطلقة وهل يوجد منهيجه في تحديد هل المحاسبة</p> <p>كيف يفشل المفوض في عملة المطلوب منه</p> <p>عدم وجود خريطة عامة لتحديد وظيفة المفوض قد يؤدي الى عدم محاسبة المتسبب او المتقاعس</p> <p>في حادث احالة محافظ بنك المركزي الى النيابة لوجود شبه تعاملات مالية بناءا على معلومات داخلية و قد تآثر السوق بهذه الحالة كيف تعامل ابوزارة و المجلس مع هذه الحادثة و هل فعلا يوجد محاسبة حقيقة</p>
<p><b><u>Disclosure regime to tackle insider trading</u></b></p>	<p>To prove the lack of understanding of the importance of the disclosure obligation to make investment decision and prevent insider trading.</p>	<p>18. Does the current disclosure obligation provide investors' confidence in kuwait stock market?</p> <p>19. Is the insufficient definition of the inside information the causes of ineffectiveness?</p> <p>20. Does the new Executive bylaw in 2015 help to improve the disclosure regime.</p> <p>21. Does investment decisions in Kuwait are based mainly on friendships and family relationships rather than financial studies or analysis?</p> <p>22. Does the list company disclosure is enough to provide investor with adequate information about the company?</p> <p>23. Does the disclosure requirement need listed company to approach advisor to ensure that they disclose the accurate information or have opinion to ensure their compliance with disclosure obligation? what about the CMA open-policy does it help?</p> <p>24. Does the disclosure provide clear picture of the company's performance?</p> <p>25. Why there is no policy statement in terms of how to regulate the regulation?</p> <p>26. Does the current policy to issue statement regarding rumours and news is practical?</p> <p>27. Can kuwait someday adopts no comments policy?</p> <p>28. Is the current practice to regulate the unusual trading activity sufficient?</p> <p>29. What if the CMA did not involve regulating the unusual trading activity?</p> <hr/> <p>30. Do the investors have confident on the CMA to ensure fair and equal access to inside information?</p>

		<p>الافصاح</p> <p>في معظم الاحوال هل المستثمر في سوق الاوراق المالية يعتمد على الافصاحات او العلاقات الاجتماعية في تحديد القرارات الاستثمارية</p> <p>هل افصاح شركات المدرجة في سوق الكويت للاوراق المالية بخصوص المعلومات الداخلية واضح وكافي للمستثمرين</p> <p>هل الافصاحات الشركات كافية لبناء قرار استثماري في السوق</p> <p>افصاحات المعلومات الداخلية يحد من التداولات المالية بناء على معلومات داخلية بالنسبة لمتطلبات الافصاح في التداولات الغير عادية و الاشاعات مجدية و تواكب افضل الممارسات هل افصاحات الشركات كافية</p> <p>هل يوجد ارشادات دورية بشأن السياسة العامة للافصاحات</p> <p>هل توجد الية معينة لفحص الافصاحات من قبل الشركات</p> <p>ماهو دور الموظفين في حال اكتشاف مخالفة في الافصاح</p> <p>هل الافصاحات تؤدي الغرض منها او تعكس اداء الشركات</p> <p>هل المستثمر يوفّر لهم معلومات و افصاحات عن الشركة بشكل كافي و مرضي و على قدم وساق</p>
<b><u>Insider trading</u></b>	<p>To prove there is insufficient procedures to protect the markets from insider trading.</p> <p>No clear definition of the inside information</p>	<p>31. Does the insider trading transaction decreased post the CML No.7 of 2010 and its amendment in 2015?</p> <p>32. Does the CML regulates insider trading to enhance trust and confident in the stock markets?</p> <p>33. Is there awareness about the harmful of insider trading to society and economy as well and how to hurt the stock market?</p> <p>-----</p> <p>هل هي ابرز التطورات و التغيرات في قوانين منع التداولات بناء على معلومات داخلية قبل وبعد قانون الهيئة 2010</p> <p>هل تعديلات على قانون الهيئة سنة 2015 ساعد على منع التداولات و الردع و محاسبة المتسبب في التداولات الداخلية</p> <p>هل المراقبة و المحاسبة الحالية للتداولات بناء على معلومات داخلية مجدية كمستثمر في سوق اوراق المالي هل تثق بقدرت الهيئة على ضبط و مراقبة التداولات بناء على معلومات داخلية</p> <p>كمسئول هل تعتقد الهيئة لديها من الادوات و العقوبات على معاقبة التداولات بناء على معلومات داخلية</p> <p>نص القانون يجيز للهيئة فرض غرامة تصل كحد اعلى الي 50 الف دينار كويتي على الرغم من ان التعاملات في وس الاوراق المالية قد يصل الى ملايين هل العقوبة رادع و توفر الحماية للمستثمر</p> <p>هل المستثمر لديه ثقافة التداول بناء على معلومات داخلية</p>
<b><u>Whistleblowing system to uncover the insider trading</u></b>	<p>No effective protection to whistleblower.</p> <p>Unrealistic protection.</p> <p>There is no specific whistleblowing</p>	<p>34. why whistle blow only focus on the crimes that already happen not in future.</p> <p>35. Does Kuwait whistleblowing regime provide <b>encouragement</b> to people to whistle blow the wrongdoing in their organisation? Important point worth highlighting is the monetary reward helps to evaluate if the Kuwait whistleblowing is effective or not. How many whistleblowing has been reported and how many whistle-blower has been reward in</p>

regime for financial markets.		<p>general and insider trading in particular? Which prove our argument that Kuwait does not provide sufficient whistleblowing regulation</p> <p>36. Is the current reward enough to encourage people to whistle blow?</p> <p>37. Does the Kuwait legal framework provide the <b>protection</b> for whistle-blower?</p> <p>38. Does Kuwait have <b>culture or awarness</b> to whistle-blow economic crimes in stock markets. Does the CMA provide adequate information about whistle blowing in financial markets?</p> <p>39. Does the people trust the Anti-corruption Authority to hold the wrongdoer to account? Or do they have expert to investigate financial crime like insider trading.</p> <p>40. Would it help if there is joint committee between KCAK and CMA to investigate the financial crime?</p> <p>41. Is there adequate information and awarness about the importance of whistleblowing programme?</p> <p>42. Does the KCAK has any communication post reporting the misconduct. The communication after the report of misconduct is very important to ensure that the whistle-blower does not treaty unfairly at work.</p> <p>43. Does the employee whistle blow the wrongdoing in their organisation? How many cases? The outcome of the cases in the Anti-corruption Authority?</p> <p>44. Does the KACA provide statics about the whistleblowing report? How many report about insider trading so far</p> <p>---</p> <p>بالنسبة لقدرة الموظفين على التبليغ عن قضايا فساد و من ضمنها التداولات بناء على معلومات داخلية ماهو دور الهيئة في تعزيز ثقافة التبليغ عن التداولات هل ورش العمل غير ملزمة للشركات كافية لتتقيف للموظفين و الافراد على الدور الفعال في التبليغ عن قضايا التداولات بناء على معلومات داخلية حماية المبلغ من اهم الضمانات الاساسية لنظام حماية ضد الفساد كموظف او فرد على الحماية و الضمانات كافية للإبلاغ عن قضايا تداولات بناء على معلومات داخلية هل الية البلاغ و الحماية واضح للموظفين في الهيئة نفسها للتصدي و التعامل مع هذه البلاغات هل يوجد تعاون بين الهيئة و بين هيئة نزاهة للمتابعة بلاغات التداولات بناء على معلومات داخلية</p>
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		<p>هل يوجد تعاون بين الهيئة و هيئة نزاهة بخصوص التحقيق في قضايا التعايلات او يتم للاستعادة بخبرة الهيئة في قضايا التدايلات</p> <p>هل حماية المبلغين باعطاء هوية جديدة مطبق او قابل للتطبيق</p>
<p><b><u>Enforcement chapter</u></b></p>	<p>The weakness of the current public enforcement which depends only on deterrence approach.</p> <p>The lack of transparency in terms of the CMA settlement agreement.</p> <p>The insufficient financial penalty.</p>	<p>45. Are the licensed firms aware of the judicial officer powers? Gathering information, the names of the officer, and the limitation of the powers?</p> <p>46. Do you think, the current financial penalty is sufficient to deterrent the non-compliance firms?</p> <p>47. Do you think the current CML No.7 of 2010 provide sufficient protection to the confidentiality agreement based on the judicial officer powers?</p> <p>48. Do you think CMA provides fair treatment in terms of the settlement agreement?</p> <p>49. Are you aware of any thematic view of the settlement agreement?</p> <p>50. Do you think Publication of the all enforcement decision without having provision in the law violate the confidently principle?</p> <p>51. Do you think its conflict of interest that the financial penalties go to the CMA <b>budget</b> as it part of its financial resource, which might cause a conflict of interests because the authority might be tempted to increase the number of financial penalties? Unlike UK system, the penalties go to the Treasury after deducting the enforcement cost, would it help to emphasis the trust of the conducted of the financial penalties go the Ministry of Commerce and Industry budget not the CMA budget?</p> <p>52. Do you think, the deterrence approach to enforce the law is the enough strategy to enforce the law, where the UK approach adopts combination of deterrence and compliance approach?</p> <p>----</p> <p>ما هي ابرز ملامح للتطور في هيئة اسواق المال بالنسبة بعد قانون 2010 بخصوص قدرت الهيئة على جمع المعلومات و التفتيش الاشخاص المرخص لهم</p> <p>هل القانون يعطي الهيئة السلطات الكافية لجمع المعلومات و التفتيش</p> <p>ما هي التطورات التي طرات بعد تعديل 2015</p> <p>الضبطية القضائية و صلاحيات موظفي الهيئة في التوصل للمعلومات كافة و هل توجد قضايا فعلا تم ضبط تدايلات او ملفات بناء على معلومات داخلية</p> <p>هل الاشخاص المرخص لهم على علم و دراية باسماء الاشخاص الذين يملكون الضبطية القضائية</p> <p>بالنسبة لقرارا الهيئة التنفيذية و العقوبات الادارية على الاشخاص المرخص لهم هل العقوبات مناسبة لفعل و تؤثر لردع للشركات علر الفعل</p>



		<p>هل سياسة العقوبات بدون اتباع سياسة التحفيز على الامتثال قادرة على توفير حماية اللازمة للأشخاص المرخص لهم</p> <p>ماهي الساسة العامة في تحديد العقوبات على الاشخاص المرخص بهم حيث ان القانون يعطي الهيئة 15 وسيلة لمعاقبة الاشخاص المرخص لهم</p> <p>هل العقوبات رادع للتداولات بناء على معلومات داخلية</p> <p>كمستثمر كون الغرامات المالية تذهب الى ميزانية الهيئة و ليس ميزانية العامة للدول على تثق بقدر لاهيئة على عدم التعسف في فرض العقوبات</p> <p>ماهو الحد والسياسة التي تحد من قدرت الهيئة على التعسف في اصدار العقوبات في ظل عدم وجود سياسة عامة واضحة منشورة لتحديد الاولويات</p> <p>هل قرارات التنفيذ المنشور و المعلومات الواردة فيها تمثل ردع في السوق</p> <p>ماهي سياسة الهيئة بخصوص الصلح مع الشركات المخلة هل يوجد الية متبعة لضمان الصلح تتبعها الهيئة</p> <p>هل قضايا الصلح 6 منشورة باسماء الشركات و الفعل المركب</p> <p>هل اجراءات الصلح تفقر ضمانه للمستثمر في السوق</p> <p>ماذا عن قضايا التداولات بناء على معيومات داخلية هل الصلح وارد فيها</p>
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