



Brokerage Business Models Outreach Conduct Supervision, Markets and Enforcement

28 March 2024

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Opening Remarks

Justin Baldacchino
Managing Director, Supervision

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- Financial Crime Supervision

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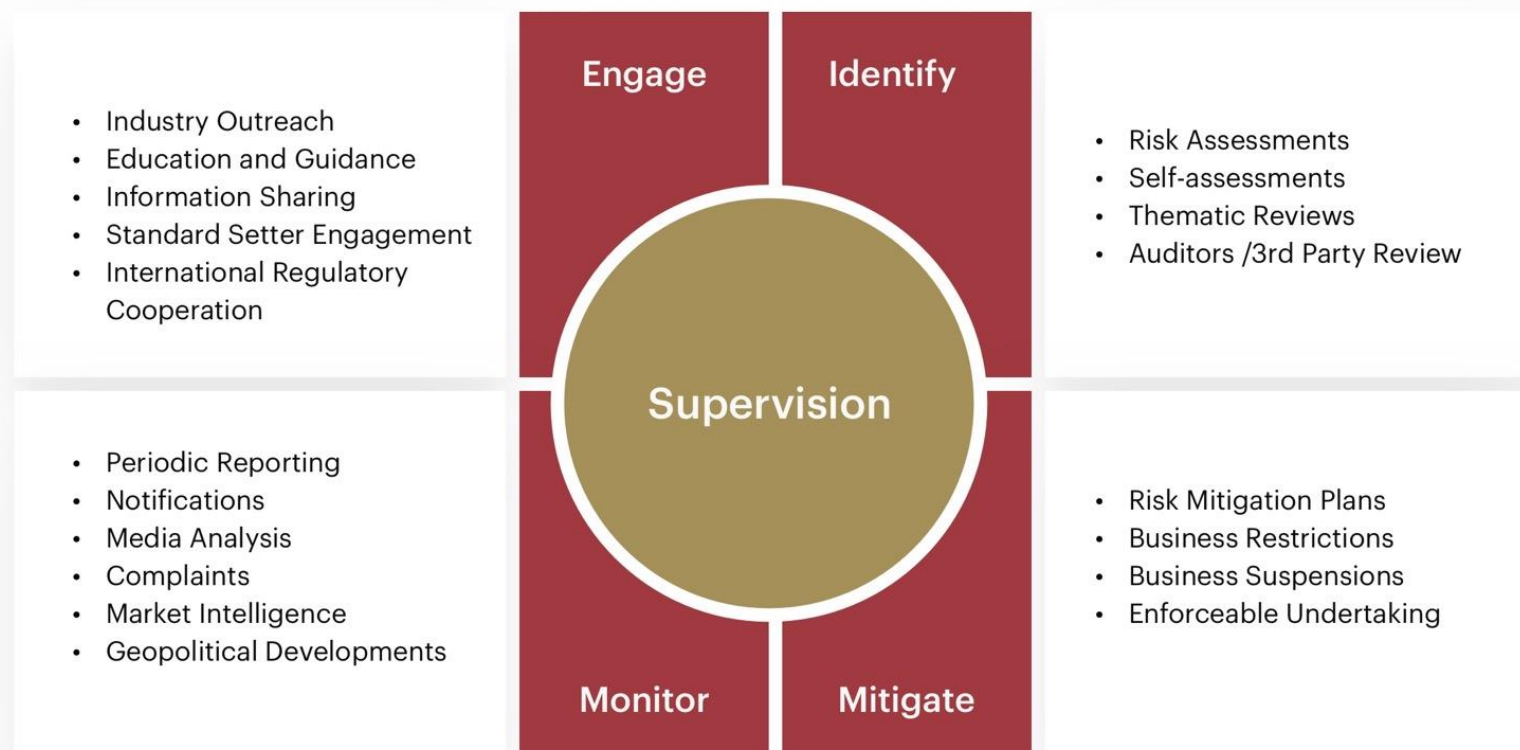
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Supervision: Background and Context

Supervision: Risk Based Supervisory Approach



Dear SEO Letter dated 18 March 2024 - Key Themes and Findings from 2023 DFSA Risk Assessments: Brokerage Business Models

Supervision: Brokerage Sector in Context

Currently 54
AFs in sector

c.12m trades
reported in
2023

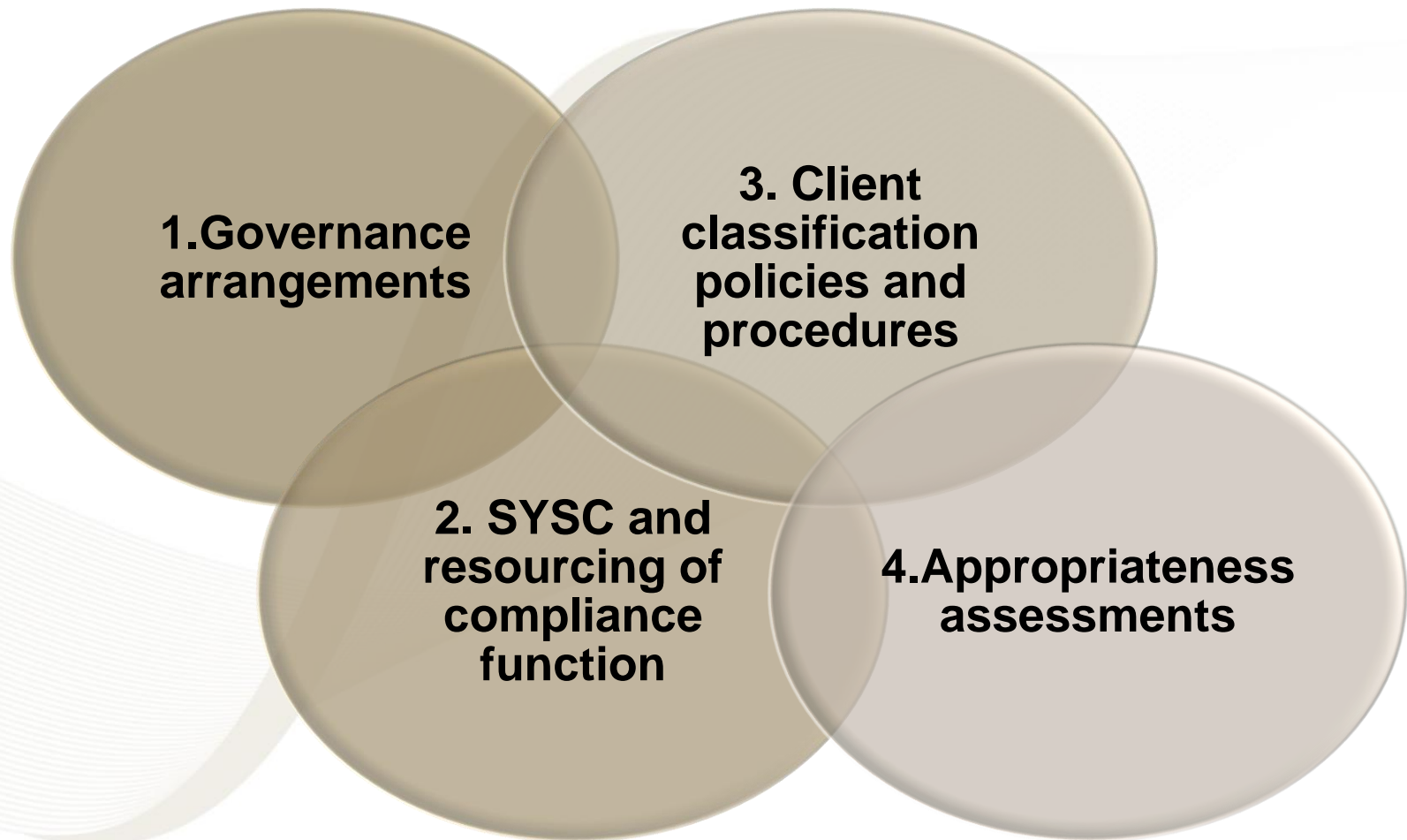
Increase in AFs
over past few
years (up c.20%
in 2023)

Healthy pipeline
of new licencing
applications



Supervision: Key Themes & Findings (Conduct)

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Supervision: Key Themes & Findings (Conduct)

**5. Remuneration
practices**

**6. Handling of
staff related
misconduct**

**7. Outsourcing
and reliance on
Group entities**

**8. Suspicious
Transaction Order
Reports**

Supervision: Key Themes & Findings (Conduct)

1. Governance arrangements – GEN 4.2.11, 5.2, 5.3.2, 5.3.3

- Issues with Board composition and lack of independent challenge.
- Lack of clarity on roles, responsibilities and reporting lines of senior management.
- Particular care needed where senior management have dual reporting lines at firm and Group level.

Actions:

- Firms must review the adequacy of their current governance arrangements to ensure they are appropriate and aligned to the nature, scale and complexity of their business activities.

Supervision: Key Themes & Findings (Conduct)

2. Systems and controls and compliance resourcing - GEN 5.3.7, 5.3.9, 5.3.11

- Inadequate resourcing levels and capacity of the compliance function.
- Inadequacies in Compliance Monitoring Programmes (gaps in coverage, absence of monitoring/testing and delays in conducting monitoring/testing activities).

Actions:

- Firms must review the adequacy of their current compliance resources, particularly in light of the pace of business growth.
- Where appropriate, firms should strengthen their compliance functions with additional resources.
- Firms should also review their Compliance Monitoring Programmes to ensure they have the right level of coverage and effective monitoring/testing is carried out.

Supervision: Key Themes & Findings (Conduct)

3. Client classification policies and procedures - COB 2

- Knowledge and experience assessments found to be unsatisfactory.
- Lack of documented rationale and/or supporting evidence.
- Over-reliance on client classification assessments performed by Head Office/Group entities without a gap analysis against local requirements.
- Lack of evidence of monitoring and challenge by compliance function.

Actions:

- Firms must review the adequacy of their client classification policies and procedures as a matter of priority.

Supervision: Key Themes & Findings (Conduct)

4. Appropriateness assessments (COB 6.16.3)

- Issues with the quality of appropriateness assessments, with potential to cause significant harm to Retail Clients.

Actions:

- Firms must review the adequacy of their appropriateness assessments as a matter of priority.

Supervision: Key Themes & Findings (Conduct)

5. Remuneration practices - GEN 4.2.12, 5.3.31, A3.2

- Fixed and variable remuneration elements not appropriately balanced, with absence of non-financial metrics.
- Remuneration policies lacking deferral and claw-back provisions.

Actions:

- Firms must review their remuneration policies and associated HR documents to ensure they are aligned with promoting a positive compliance culture and good market conduct by brokers.

Supervision: Key Themes & Findings (Conduct)

6. Handling of staff related misconduct - GEN 5.3.18/5.3.19

- Failure to give appropriate weight or consideration to previous misconduct.
- Failure to notify DFSA where significant breach of our rules by staff.
- Delays in dealing with staff misconduct or failure to take any disciplinary action at all.
- Deficiencies in implementing compliance training for staff.

Actions:

- Firms must review their systems and controls relating to staff and agents. This includes HR disciplinary processes and staff training programs.

Supervision: Key Themes & Findings (Conduct)

7. Outsourcing & reliance on Group entities - GEN 5.3.21

- Failure to properly tailor Group policies and procedures to meet local/DFSA requirements.
- Relevant DIFC staff not demonstrating an adequate understanding or oversight of functions outsourced to Group entities.
- Outdated SLAs, lacking in detail, or not reflective of services being provided in practice.

Firms are reminded they cannot outsource their regulatory obligations on outsourcing and remain accountable.

Actions:

- Firms must review their contractual/oversight arrangements of key functions or activities outsourced to Group entities and ensure they meet DFSA requirements.



Markets Team:

8. Suspicious Transaction and Order Reports (STORs)

Markets Team:

8. Suspicious Transaction and Order Reports

If conduct occurs in, from or affects DIFC markets or users of DIFC markets.

Relevant provisions:

- ❖ Markets Law 2012 Part 8 – Chapter 1 and 2
- ❖ GEN 5.3.20 and 11.10.12A

Requirements:

Entities must inform the DFSA immediately if it:

- Receives an order, or arranges or executes a transaction; and,
- Has **reasonable grounds** to suspect that the order or transaction may constitute Market Abuse.

How to notify the DFSA:

- ✓ Through the online portal.

Markets Team:

8. Suspicious Transaction and Order Reports

Concerns identified were:

1. Lack of
STOR
submissions

2. Quality of
STOR
submissions

3. Outsourcing

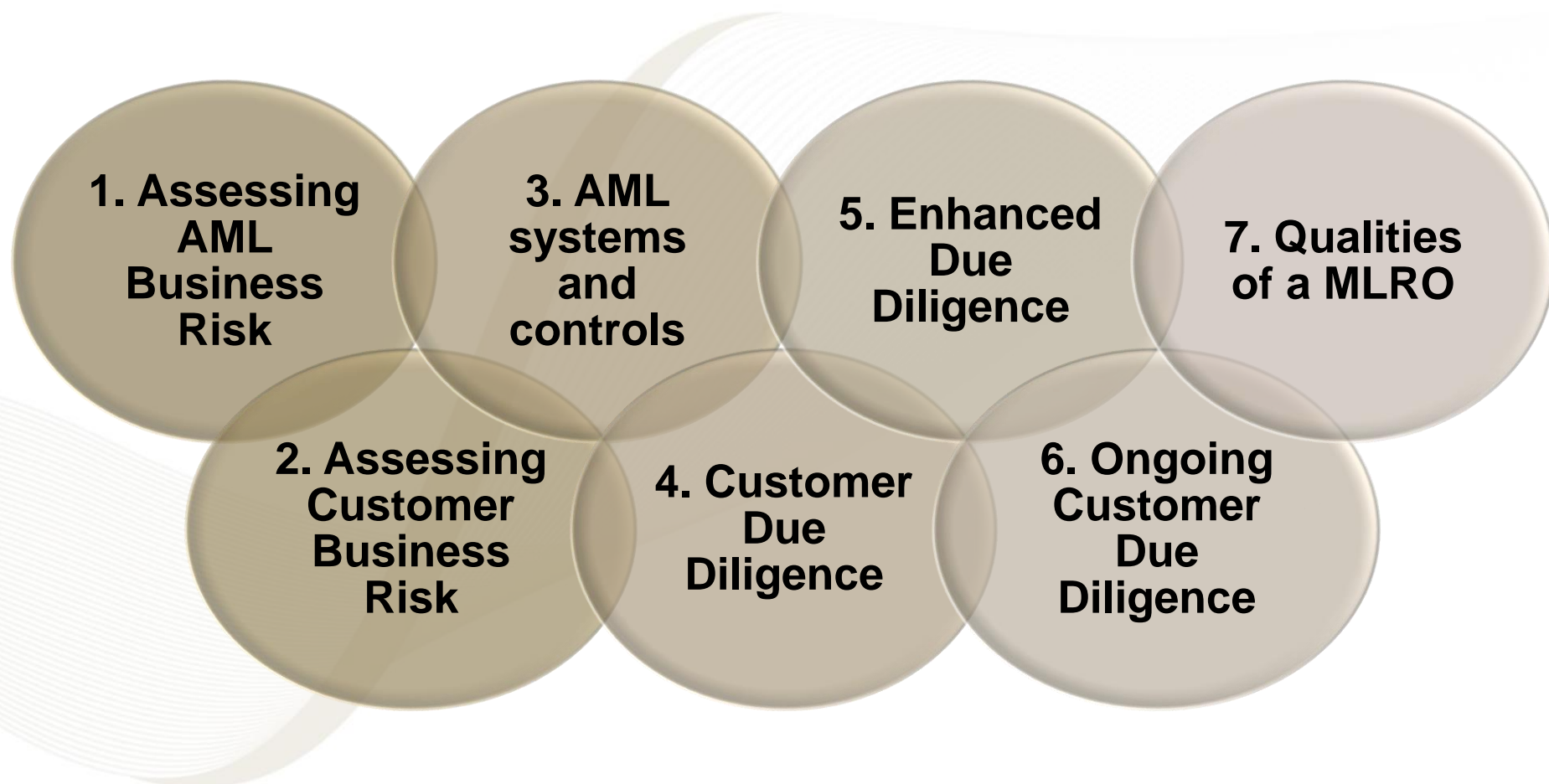
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SYSC

Actions:

- Firms must have systems and controls in place to prevent and detect market abuse and to notify the DFSA immediately if they suspect that an order or transaction may constitute market abuse, through submission of a STOR.

Supervision: Key Themes & Findings (Financial Crime)

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Supervision: Key Themes & Findings (Financial Crime)



1. Assessing Business AML Risks – BARA - AML 5.1

- Lack of a clear business risk assessment and scoring methodology.
- Reliance on wider Group methodology without understanding how it is applied in the DIFC.
- No inherent risk, controls effectiveness and/or residual risk ratings.
- Too generic and not sufficiently granular.
- No consideration of quantitative data to support inherent risk results.
- Failure to include an assessment of TFS (including PF) risk.
- Not considering the UAE NRA outcomes.

Actions:

- Firms are reminded of their obligation to take appropriate steps to identify and assess money laundering, terrorist financing and proliferation financing risks to which its business is exposed, taking into consideration the nature, size and complexity of its activities as set out in AML 5.1.

Supervision: Key Themes & Findings (Financial Crime)

2. Assessing Customer AML Risks - AML 6.1

- No clear correlation between the ABRA, Customer Risk Assessment and the client risk profile.
- Unclear customer risk assessment / scoring methodology.

Actions:

- Firms must establish an appropriate customer risk assessment framework.

Supervision: Key Themes & Findings (Financial Crime)

3. AML systems and controls - AML 5.2

- AML policy and procedures were out of date.
- AML policy and procedures for some firms not customised to the firm's business activities and processes.
- Reliance placed on group Sanctions procedures but lacking detailed local operational procedures to comply with the UAE TFS requirements.
- Lack of Management Information / metrics covering key AML processes, hampering effective local senior management oversight.

Actions:

- Firms should ensure they establish and maintain effective AML policies, procedures, systems, and controls which are tailored to the nature, scale, and complexity of its business activities.

Supervision: Key Themes & Findings (Financial Crime)

4. Customer Due Diligence - AML 7.3

- Failure to consistently or appropriately implement Customer Due Diligence measures.
- Common findings observed were in relation to the identification and verification of:
 - Customers;
 - Beneficial owners; and
 - Addresses.

Actions:

- Firms to implement robust CDD procedures, including identification and verification of customers and any beneficial owners, to ensure compliance by relevant employees responsible for conducting customer due diligence.

Supervision: Key Themes & Findings (Financial Crime)

5. Enhanced Customer Due Diligence - AML 7.4

- Deficiencies in corroboration of source of funds (SOF) and source of wealth (SOW) for high-risk clients.
- Common findings observed:
 - limited SOW journey narratives; and
 - lack of supporting evidence documents.

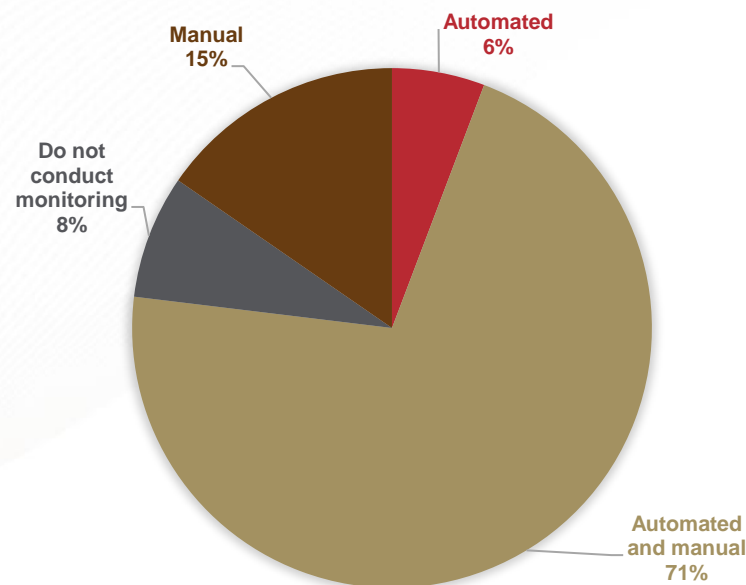
Actions:

- Firms to implement robust EDD procedures, including appropriate corroboration steps, and to ensure compliance by relevant employees responsible for conducting customer due diligence and those approving high risk client files.

Supervision: Key Themes & Findings (Financial Crime)

6. Ongoing Customer Due Diligence - AML 7.6

- Process applied not appropriate given the size and nature of the firm's business, its customer base, complexity, and volume of customer transactions.
- Ineffective performance of periodic CDD reviews – outdated ID&V documents and absence of commentary on transactional activity patterns.



Actions:

- DFSA expects firms to implement effective procedures, systems and controls, and monitoring mechanisms to ensure ongoing customer due diligence is conducted effectively and in a timely manner.

Supervision: Key Themes & Findings (Financial Crime)

7. Quality of a MLRO - AML 11.3

- 65% of MLRO functions are in-house functions.
- We observed instances where, given the nature, size and complexity of the firm's business, its customer base and volume of transactions, the MLRO did not have sufficient resources to assist in the performance of his/her duties in an effective, objective and independent manner.

Actions:

- Firms must review the adequacy of their current AML resources to ensure that their systems and controls are appropriate to the nature and extent of the firm's business, including the pace of business growth. Where appropriate, firms should strengthen their AML functions by increasing resources.



Enforcement Update

Patrick Meaney
Managing Director, Head of Enforcement

Enforcement Update

Case Study 1 – Bank of Singapore Limited (BOS) – Findings

- Inadequate:
 - AML risk assessments and client risk ratings;
 - Customer Due Diligence (CDD) and Enhanced CDD practices;
 - Identification of Clients' sources of wealth and sources of funds;
 - Suspicious Activity Reporting.
- Also acted outside scope of licence (Long Term Insurance contracts).

Enforcement Update

Case Study 1 – Bank of Singapore Limited (BOS) - Outcome

- November 2022 fined USD 1,120,000 – reduced from USD 1.6 million due to 30% settlement discount.
- Enforceable Undertaking (EU):
 - Undertake remediation exercise;
 - Engage external compliance expert to assist with and verify remediation.

Enforcement Update

Case Study 2 – Mirabaud (Middle East) Limited – Findings

- AML systems and controls did not pick up (nor report) possible layering activity:
 - Nine interconnected Client accounts;
 - Same Relationship Manager;
 - Accounts operated by same group of individuals;
 - Funds deposited from third party accounts;
 - Funds transferred to companies with opaque ownership structures and bank account in unrelated jurisdictions.
 - For commercial purposes even though bank policy did not allow
 - Funds flowing repeatedly between connected entities.

Enforcement Update

Case Study 2 – Mirabaud (Middle East) Limited – Outcome

- Fine USD 3,022,500 – July 2023.
- Included disgorgement of USD 975,000.
- Settlement therefore 30% discount.

Enforcement Update

Case Study 3 – FFA Private Bank (Dubai) Limited – Findings

- Inadequate systems and controls to identify, assess and report suspicious trading;
- Limited STORs filed with DFSA;
- Possible facilitation of market abuse;
- Much of the trading by the two Clients was suspicious;
- FFA outsourced monitoring of Client trading but failed to effectively supervise.

Enforcement Update

Case Study 3 – FFA Private Bank (Dubai) Limited — Outcome

- Fine USD 373,842 – November 2023.
- Settlement therefore 30% discount.

Enforcement Update

Case Study 4 – R.J. O'Brien (MENA) Capital Limited – Findings

- Inadequate compliance systems and controls;
- Firm acquired another broker firm;
- Failed to analyse and plan for the additional compliance resources required;
- Senior management aware of the lack of compliance resources - failed to address the issue;
- Clients allowed to trade before onboarding completed;
- RM used an unauthorized method to communicate with clients
 - was not disciplined for it at the time it was discovered.

Enforcement Update

Case Study 4 – R.J. O'Brien (MENA) Capital Limited – – Outcome

- Fine USD 1,368,767 – December 2023.
- Settlement therefore 30% discount.
- Private Warning Letter issued to an individual.

Enforcement Update

Lessons Learned from 2023 Enforcement Actions

- Proper KYC, CDD and EDD checks, including source of wealth, need to be comprehensive and timely;
- All possible sources of information about a client should be searched when setting customer risk ratings;
- High variable remuneration based on revenue generation creates compliance risks that require a risk mitigation strategy;
- Compliance and risk management functions need to be adequately resourced both in terms of skills and headcount and have a strong voice – they should not be easily overruled by the business;
- Senior management are responsible ensuring compliance and should view their compliance staff as advisers assisting them to discharge this responsibility; and
- Non-compliant staff should be disciplined appropriately.



Q&A



Closing Remarks

Patrick Meaney
Managing Director, Head of Enforcement

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Thank you!