



**By Email**

15 December 2023

To: Senior Executive Officers (SEO) of Money Services Firms

**Re: Thematic review findings - Money Services Firms safeguarding of Client Money**

Dear SEO,

The purpose of this letter is to update you on our findings and observations from a recent thematic review (“**Thematic Review**”) of Authorised Money Services Firms’ (“**MS Firms**”) systems and controls to safeguard Client Money. We wish to thank the MS Firms who participated in the Thematic Review for their cooperation.

Unless the context requires otherwise, capitalised terms used in this letter have the same meaning as set out in the Glossary Module of the DFSA Rulebook.

**Background**

In April 2023, the DFSA requested MS Firms to provide information about their Client Money safeguarding policies, procedures, systems and controls to:

- (1) assess compliance with DFSA Client Money Rules; and
- (2) evaluate the adequacy of Firms’ systems and controls to identify and mitigate risks associated with holding or controlling Client Money.

The Annex to this letter contains the key findings and observations from the Thematic Review.

While the findings are specific to participating MS Firms, the DFSA expects all Authorised Firms holding or controlling Client Money to continually assess their Client Money policies, procedures, systems and controls, and implement appropriate actions where necessary to ensure they operate in a regulatory compliant manner. The DFSA has also provided specific feedback, including Risk Mitigation Programmes where necessary, to individual Firms to address areas of non-compliance with the Rulebook.

If you have any questions in relation to this letter, please contact us using the DFSA Supervised Firm Contact Form found on the [DFSA ePortal](#).

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Justin Baldacchino', is written over a light blue horizontal line.

**Justin Baldacchino**  
**Managing Director, Supervision**

CC: Compliance Officers & Finance Officers of Authorised Money Services Firms

## **Annex - Key findings and observations**

Below are the key findings and observations from the Thematic Review, highlighting where improvements are needed to align with the DFSA Client Money Rules.

Please keep in mind these are thematic findings and are common to multiple but not all MS Firms.

### **1. Client Accounts**

The majority of MS Firms were able to demonstrate that they maintained a master list of all Client Accounts (holding Client Money) held with Third Party Agents (the **Master List**) in accordance with Rule A5.4.2 of the COB Module (COB) of the Rulebook.

We identified some instances, where the Master List did not contain all the relevant information, such as the location of the account, open or closed status, date of opening, or closure (as appropriate), as required under COB A5.4.2. Additionally, certain MS Firms failed to demonstrate that they maintained a Master List and instead presented a list of all accounts the firm, itself, had opened for Clients, not Third Party Agents.

MS Firms are required to maintain a Master List and must ensure all required details are included in that Master List as stipulated in COB A5.4.2. MS Firms must also ensure they regularly review these Master Lists to ensure they are accurate and current.

### **2. Appointment of a Third Party Agent**

Our review revealed that most MS Firms conducted suitability assessments prior to appointing a Third-Party Agent as required by COB A5.6. However, we identified instances where MS Firms failed to undertake a suitability assessment before appointing a Third Party Agent to hold Client Money. Certain MS Firms also failed to demonstrate the existence of adequate systems and controls to ensure the appointed Third Party Agents remain suitable.

MS Firms are required to undertake an initial suitability assessment of all Third Party Agents before establishing a Client Account with them, and demonstrate the implementation of adequate systems and controls to ensure those Third Party Agents remains suitable.

MS Firms opening a Client Account with a Third Party Agent must also obtain a written acknowledgement from that Third Party Agent that it will apply the protections stipulated in COB A5.7.2 in relation to the Client Account. This includes a confirmation that the MS Firm is holding Client Money as an agent and the Third Party Agent is not entitled to combine the account with other accounts or to exercise any charge, mortgage, lien, right of set-off or counterclaim against money in that Client Account in respect of any sum owed to it on any other account of the MS Firm. However, we identified instances where certain Firms failed to obtain this letter.

MS Firms must ensure they obtain this written acknowledgment prior to using the Client Account.

### **3. Payment of Client Money into Client Accounts**

MS Firms are not permitted to commingle their own money with Client Money. The majority of MS Firms were generally able to demonstrate that they had appropriate systems and controls to prevent the comingling of their money with Client Money. Those MS Firms were also able to

demonstrate, via their policies and procedures, that the limited circumstances where the MS Firm did deposit its own money into a Client Account, complied with COB A5.3.3. For example, depositing sums in Client Accounts to meet a minimum sum required to open or keep open a Client Account, or to meet shortfalls in Client Money held in that Client Account.

However, we identified instances where certain MS Firms failed to incorporate COB A5.3.3 requirements in their Client Money policies and procedures. Such an omission creates a risk the MS Firm may inadvertently deposit its own money into a Client Money Account, thereby failing to properly safeguard Client Money and demonstrate compliance with DFSA Client Money Rules.

MS Firms' Client Money policies and procedures should outline all exceptions where the firm's own money is permitted to be deposited into Client Accounts in compliance with DFSA Client Money Rules.

#### **4. Client disclosure**

MS Firms holding Client Money must make certain disclosures to the Clients on whose behalf the Client Money is held, as set out in COB A5.9. The DFSA identified instances where certain MS Firms did not provide all of the required disclosures set out in COB A.5.9. In particular, certain MS Firms failed to demonstrate disclosure to their Clients of Client Money being held in a Client Account with a Third Party Agent. Certain MS Firms also failed to disclose the basis and terms governing the way in which the Client Money will be held, or whether interest was payable to the Client and relevant terms.

MS Firms must ensure they make adequate and suitable disclosures to Clients on how Client Money is held on the Clients' behalf, the basis and terms governing the way in which the Client Money is held, and the protections available to the Client under DFSA Client Money Rules.

#### **5. Client reporting**

The COB Rules require MS Firms to provide statements to their Clients setting out details of Client Money held on the Clients' behalf, including details of all credits and debits. The majority of MS Firms were able to demonstrate compliance with the Client reporting requirements in COB A5.10. In all instances where statements were provided to Clients, those statements were provided monthly (for retail clients) or agreed intervals (for professional clients). However, we identified instances where certain MS Firms failed to provide these statements to their Clients.

MS Firms must ensure that all of their Clients are provided with Client Money statements that outline the balances, credits, debits, interest earned or charged on the Client Account, and other relevant information, as mandated by COB Rule A5.10.

#### **6. Reconciliation**

Our review revealed that all participating MS Firms reconciled their Client Money balances in accordance with COB A5.11. Whilst COB A5.11.1 mandates Client Account reconciliation at least every 25 days, we observed that certain MS Firms reconciled their Client Accounts more frequently, with some as frequent as daily.

During the Thematic Review, the DFSA introduced COB A5.11.1(5) which applies to Authorised Firms that Provide Money Services and requires those firms to complete accurate reconciliations

of Client Accounts at least daily. Accordingly, MS Firms must update their Client Money policies, procedures, systems and controls to operationalise these new requirements and ensure senior management and relevant staff are made aware of these new requirements.

## **7. Auditor's Report**

COB A5.12 requires MS Firms to submit a Client Money Auditor's Report on an annual basis. Our review revealed that all participating MS Firms had submitted a Client Money Auditor's Report. However, we identified instances where certain MS Firms failed to submit their Client Money Auditor's Report within the required timeframe.

MS Firms must ensure their Client Money Auditor's Report is provided annually and within the required timeframe.

## **8. Client Money distribution rules**

Following a Distribution Event, MS Firms must distribute money in accordance with the order of priorities set out in COB A.5.13. In particular, these distribution rules outline how Client Money is distributed to Clients, the order of priorities for that distribution, and how to approach situations where there are insufficient funds in the Client Account to satisfy amounts due to Clients.

Our review revealed that most MS Firms have implemented policies and procedures outlining how money is to be distributed in the event of a Distribution Event, and which included explicit references to COB A5.13. However, we identified instances where certain MS Firms failed to incorporate COB A5.13 requirements in their Client Money policies and procedures. Such omissions create a risk of Client Money being distributed in breach of COB A5.13 and thereby undermining the Client Money protections in the DFSA Rules.

MS Firms must ensure their Client Money policies and procedures incorporate the COB A5.13 requirements and are applied without deviation following a Distribution Event.

## **9. Breaches**

COB A5.14.1 requires MS Firms to notify the DFSA within one day of becoming aware that it does not comply with the DFSA Client Money Rules. Our review revealed most MS Firms maintain a Client Money Breach Register which they use to track and monitor breaches of Client Money Rules. However, we identified instances where certain Breach Registers had omitted the date of the relevant breach which prevented an accurate assessment of that firm's compliance with COB A5.14.1. There were also instances where MS Firms failed to evidence appropriate oversight and tracking of Client Money breaches to demonstrate compliance with COB A5.14.1.

MS Firms are required to implement appropriate systems and controls to ensure they identify, record, and notify the DFSA of any breach of Client Money Rules within the one day limit.

## **10. Records Management**

COB 6.12.5, COB A5.4.2 and COB A5.5.3 require MS Firms to maintain certain Client Money records for a minimum of six years. Our review revealed that the majority of MS Firms incorporated these record keeping requirements in their Client Money policies and procedures and implemented systems and controls to ensure records are retained for this period. However,

we identified instances where certain Client Money policies and procedures did not include this requirement.

MS Firms must update their Client Money policies and procedures and implement appropriate systems and controls to ensure that Client Money record keeping requirements are met.

## **11. Client Money policies and procedures**

While all participating MS Firms provided the DFSA with their Client Money policies and procedures, the DFSA observed that several of these policies and procedures failed to reference relevant DFSA Rules. For example, certain of these policies and procedures failed to articulate when and in what circumstances the firm may deposit its own funds into Client Accounts and that Client Money belonging to one Client cannot be used to satisfy obligations owed to another Client. Additionally, certain policies failed to refer to the specific business model and activity of the firm and were generic, 'off the shelf', documents.

MS Firms must ensure they review and update their Client Money policies and procedures to ensure they incorporate all relevant requirements in the DFSA Rules on a continuing basis.

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