

Appendix 1

In this appendix underlining indicates new text and striking through indicates deleted text.



The DFSA Rulebook

Conduct of Business Module

(COB)

6.11 Client Assets

Application

6.11.1 This section applies to an Authorised Firm which:

- (a) holds or controls Client Assets; or
- (b) Provides Custody or Arranges Custody.

Guidance

1. Client Assets is defined in the GLO Module as “Client Money and Client Investments”.
2. Principle 9 of the Principles for Authorised Firms (Customer assets and money) requires an Authorised Firm to arrange proper protection for clients' assets when the firm is responsible for them. An essential part of that protection is that an Authorised Firm must properly safeguard Client Money and Client Investments held or controlled on behalf of a Client in the course of, or in connection with, the carrying on of Investment Business in or from the DIFC.
3. An Authorised Firm must introduce adequate organisational arrangements to minimise the risk of the loss or diminution of Client Assets, or of rights in connection with Client Assets, as a result of the Authorised Firm or a third party's insolvency, fraud, poor administration, inadequate record-keeping or negligence.

General requirements

- 6.11.2**
- (1) An Authorised Firm which holds or controls Client Money must comply with sections 6.12 and 6.14.
 - (2) An Authorised Firm which holds or controls Client Investments, or Provides Custody or Arranges Custody must comply with sections 6.13 and 6.14.
- 6.11.3**
- (1) An Authorised Firm must have systems and controls to ensure that Client Assets are identifiable and secure at all times.
 - (2) Where the Authorised Firm holds a mandate, or similar authority over an account with a third party, in the Client's own name, its systems and controls must:
 - (a) include a current list of all such mandates and any conditions placed by the Client or by the Authorised Firm on the use of the mandate;
 - (b) include the details of the procedures and authorities for the giving and receiving of instructions under the mandate; and
 - (c) ensure that all Transactions entered into using such a mandate are recorded and are within the scope of the authority of the Employee and the Authorised Firm entering into such Transactions.

Guidance

Authorised Firms are reminded that they must ensure that their auditor produces a Client Money Auditor's Report and a Safe Custody Auditor's Report as applicable, in accordance with GEN 8.6.

Holding or controlling client assets

6.11.4 Client Assets are held or controlled by an Authorised Firm if they are:

- (a) directly held by the Authorised Firm;
- (b) held in an account in the name of the Authorised Firm; or
- (c) held by a Person, or in an account in the name of a Person, controlled by the Authorised Firm.

Guidance

- 1 For the purposes of Rule 6.11.4, the DFSA would consider a Person to be controlled by an Authorised Firm if that Person is inclined to act in accordance with the instructions of the Authorised Firm.
2. The DFSA would consider an account to be controlled by an Authorised Firm if that account is operated in accordance with the instructions of the Authorised Firm.

6.12 Client money

6.12.1 All Money held or controlled on behalf of a Client in the course of, or in connection with, the carrying on of Investment Business in or from the DIFC is Client Money, except Money which is:

- (a) held by the Authorised Firm as a Bank in an account with itself, provided the Authorised Firm notifies the Client in writing that the Client Money is held by it as a Bank and not in accordance with this chapter;
- (b) immediately due and payable by the Client to the Authorised Firm;
- (c) belonging to another Person within the Authorised Firm's Group unless that Person is an Authorised Firm or Regulated Financial Institution and that Person has confirmed to the Authorised Firm, in writing, that the beneficial owner of the Money is a Person who is not part of the Authorised Firm's Group;
- (d) in an account in the Client's name over which the Authorised Firm has a mandate or similar authority and who is in compliance with Rule 6.11.3 (2);
- (e) received in the form of a cheque, or other payable order, made payable to a third party other than a Person or account controlled by the Authorised Firm, provided the cheque or other payable order is intended to be forwarded to the third party within 1 business day of receipt; or

(f) Fund Property of a Fund.

Guidance

1. Authorised Firms are reminded that the exemption in Rule 6.12.1(a) would not apply to Money which is passed to a third party i.e. not held in an account with the Authorised Firm itself.
2. Pursuant to Rule 6.12.1(b), examples of Money which is immediately due and payable to an Authorised Firm includes Money which is:
 - a. paid by the way of brokerage, fees and other charges to the Authorised Firm or where it is entitled to deduct such remuneration from the Client Money held or controlled;
 - b. paid by the Authorised Firm in relation to a Client purchase or in settlement of a margin payment in advance of receiving a payment from the Client; or
 - c. owed by the Client to the Authorised Firm in respect of unpaid purchases by or for the Client if delivery of Investments has been made to the Client or credited to his account.
3. The CIR module contains specific provisions relating to the handing of Fund Property and also provisions relating to a Fund Administrator holding or controlling monies or assets belonging to third parties.

Client money provisions

- 6.12.2**
- (1) Subject to (2), an Authorised Firm which holds or controls Client Money for a Client must comply with the Client Money Provisions in App5.
 - (2) Where the Client is a Market Counterparty, An an Authorised Firm may exclude the application of the Client Money Provisions but only where it has obtained the prior written consent of ~~a Professional Client~~ the Market Counterparty to do so.

Guidance

In accordance with GEN chapter 8, an Authorised Firm which holds or controls Client Money must arrange for a Client Money Auditor's Report to be submitted to the DFSA on an annual basis.

Client disclosure

- 6.12.3**
- (1) If an Authorised Firm holds or controls Client Money which is not subject to the Client Money Provisions pursuant to Rule 6.12.2 (2), it must disclose to that Client Market Counterparty in writing that:
 - (a) the protections conferred by the Client Money Provisions do not apply to such Client Money;
 - (b) as a consequence of (a), such Client Money may be mixed with Money belonging to the Authorised Firm, and may be used by the Authorised Firm in the course of the Authorised Firm's business; and

- (c) in the event of insolvency, winding up or other Distribution Event stipulated by the DFSA:
 - (i) in the case of a Domestic Firm, such Client Money will be subject to and distributed in accordance with the DFSA Client Money Distribution Rules; and
 - (ii) in the case of a non-Domestic Firm, such Client Money will be subject to a regime which may differ from the regime applicable in the DIFC.
- (2) The Authorised Firm must obtain that Client's Market Counterparty's written acknowledgement of the disclosures made in (1) prior to holding or controlling Client Money for that ~~Client~~ Market Counterparty.

Distribution event

- 6.12.4** Following a Distribution Event, an Authorised Firm must comply with the Client Money Distribution Rules and all Client Money will be subject to such Rules.

Record keeping

- 6.12.5** (1) An Authorised Firm must maintain records:
- (a) which enable the Authorised Firm to demonstrate compliance with Rule 6.11.2;
 - (b) which enable the Authorised Firm to demonstrate and explain all entries of Money held or controlled in accordance with this chapter; and
 - (c) of all cheques received and forwarded in accordance with Rule 6.12.1(e).
- (2) Records must be kept for a minimum of six years.

Guidance

The DFSA expects an Authorised Firm to maintain proper books and accounts based on the double-entry booking principle. They should be legible, up to date and contain narratives with the entries which identify and provide adequate information about each transaction. Entries should be made in chronological order and the current balance should be shown on each of the Authorised Firm's ledgers.

6.13 Client investments

- 6.13.1** An Authorised Firm must treat all Investments held or controlled on behalf of a Client in the course of, or in connection with, the carrying on of Investment Business as Client Investments.

6.13.2 An Authorised Firm which holds or controls Client Investments must have systems and controls in place to ensure the proper safeguarding of Client Investments.

Guidance

Instead of safeguarding Client Investments, an Authorised Firm may choose to safeguard Client Money equal to the value of the Client Investments.

6.13.3 (1) Subject to (2), an Authorised Firm:

(a) holding or controlling Client Investments;

(b) Providing Custody; or

(c) Arranging Custody

in or from the DIFC must do so in accordance with the Safe Custody Provisions in App6.

(2) The Safe Custody Provisions in App6 do not apply to Client Investments held as Collateral unless stated otherwise.

Holding collateral

6.13.4 Before an Authorised Firm holds Collateral from a Client it must disclose to that Client:

(a) the basis and any terms governing the way in which the Collateral will be held, including any rights which the Authorised Firm may have to realise the Collateral;

(b) if applicable, that the Collateral will not be registered in that Client's own name;

(c) if applicable, that the Authorised Firm proposes to return to the Client Collateral other than the original Collateral, or original type of Collateral; and

(d) that in the event of the insolvency, winding up or other Distribution Event stipulated by the DFSA:

(i) of a Domestic Firm, any excess Collateral will be sold and the resulting Client Money shall be distributed in accordance with the DFSA Client Money Distribution Rules; or

(ii) of a non-Domestic Firm, that Collateral will be subject to a regime which may differ from the regime applicable in the DIFC.

6.13.5 Before an Authorised Firm deposits Client's Collateral with a third party it must notify the third party that:

(a) the Collateral does not belong to the Authorised Firm and must therefore be held by the third party in a segregated client account in

a name that clearly identifies it as belonging to the Authorised Firm's clients; and

- (b) the third party is not entitled to claim any lien or right of retention or sale over the Collateral except to cover the obligations owed to the third party which gave rise to that deposit, pledge, charge or security arrangement or any charges relating to the administration or safekeeping of the Collateral.

6.13.6 (1) An Authorised Firm may only permit Client's Collateral to be held by a third party where it has reasonable grounds to believe that the third party is, and remains, suitable to hold that Collateral.

- (2) An Authorised Firm must be able to demonstrate to the DFSA's satisfaction the grounds upon which it considers the third party to be suitable to hold Client's Collateral.

6.13.7 (1) An Authorised Firm must take reasonable steps to ensure that the Collateral is properly safeguarded.

- (2) An Authorised Firm must withdraw the Collateral from the third party where the Collateral is not being properly safeguarded unless the Client has indicated otherwise in writing.

6.13.8 An Authorised Firm holding Client's Collateral must send a statement every six months to the Client in accordance with section A6.8.

6.13.9 An Authorised Firm must reconcile the Client's Collateral in accordance with section A6.9.

6.14 Record keeping

6.14.1 (1) An Authorised Firm must maintain records:

- (a) which enable the Authorised Firm to demonstrate compliance with Rule 6.11.2; and
- (b) which enable the Authorised Firm to demonstrate and explain all entries of Client Investments and Collateral held or controlled in accordance with this chapter.

- (2) Records must be kept for a minimum of six years.

APP5 CLIENT MONEY PROVISIONS

A5.1 Application

A5.1.1 This appendix applies to an Authorised Firm, in accordance with Rule 6.12.2

A5.2 General requirements

A5.2.1 (1) The provisions of this appendix are referred to as the Client Money Provisions.

(2) The types of Client described in Rule 6.12.2 are referred to in this appendix as Segregated Clients.

A5.2.2 An Authorised Firm which holds or controls Client Money for a Segregated Client must:

- (a) comply with the Client Money Provisions in relation to that Client Money; and
- (b) have systems and controls in place to be able to evidence compliance with the Client Money Provisions.

A5.3 Payment of client money into client accounts

A5.3.1 Where an Authorised Firm holds or controls Client Money it must ensure, except where otherwise provided in section A5.5 that the Client Money is paid into one or more Client Accounts within one day of receipt.

A5.3.2 Subject to Rule A5.3.3, an Authorised Firm must not deposit its own Money into a Client Account.

A5.3.3 (1) An Authorised Firm may deposit its own Money in a Client Account where:

- (a) it is a minimum sum required to open the account, or to keep it open;
- (b) the Money is received by way of mixed remittance provided the Authorised Firm transfers out that part of the payment which is not Client Money within one day of the day on which the Authorised Firm would normally expect the remittance to be cleared;
- (c) interest credited to the account exceeds the amount payable to Segregated Clients, provided that the Money is removed within twenty five days; or

(d) it is to meet a shortfall in Client Money.

(2) Where an Authorised Firm deposits its own Money into a Client Account such Money is Client Money until such time as the Money is withdrawn from the Client Account in accordance with the Client Money Provisions.

A5.3.4 An Authorised Firm must maintain systems and controls for identifying Money which must not be in a Client Account and for transferring it without delay.

A5.3.5 Where an Authorised Firm is aware that a Person may make a payment of Client Money to the Authorised Firm, it must take reasonable steps:

- (a) to ensure that such payment of Client Money is directed to a Client Account; and
- (b) to ensure that the Authorised Firm is notified by that Person of such payment as soon as reasonably practicable.

Guidance

An Authorised Firm should have procedures for identifying Client Money received by the Authorised Firm, and for promptly recording the receipt of the Money either in the books of account or a register for later posting to the Client cash book and ledger accounts. The procedures should cover Client Money received by the Authorised Firm through the mail, electronically or via agents of the Authorised Firm or through any other means.

A5.4 Client accounts

A5.4.1 A Client Account in relation to Client Money is an account which:

- (a) is held with a Third Party Agent;
- (b) is established to hold Client Assets;
- (c) is maintained in the name of;
 - (i) if a Domestic Firm, the Authorised Firm; or
 - (ii) if a non-Domestic Firm, a Nominee Company controlled by the Authorised Firm; and
- (d) includes the words 'Client Account' in its title.

A5.4.2 (1) An Authorised Firm must maintain a master list of all Client Accounts.

- (2) The master list must detail:
- (a) the name of the account;
 - (b) the account number;

- (c) the location of the account;
 - (d) whether the account is currently open or closed; and
 - (e) the date of opening or closure.
- (3) The details of the master list must be documented and maintained for at least six years following the closure of an account.

Guidance

1. An Authorised Firm may hold or control Client Money belonging to a Segregated Client in a Client Account solely for that Client. Alternatively, an Authorised Firm may choose to pool that Client Money in a Client Account containing Client Money of more than one Segregated Client.
2. The purpose of controlling or holding Client Money in a Client Account is to ensure that Money belonging to Segregated Clients is readily identifiable from Money belonging to the Authorised Firm such that, following a Distribution Event, Segregated Clients will rank highest in line in terms of any subsequent distribution of Client Money in proportion to each Client's valid claim over that that Money.
3. Following a Distribution Event, a Segregated Client ~~will~~ may not have a valid claim over Client Money held or controlled in a Client Account if that Client Account was not established to hold or control Client Money for that Client or pool of Clients.

A5.5 Exceptions to holding client money in client accounts

A5.5.1 The requirement for an Authorised Firm to pay Client Money into a Client Account does not, subject to Rule A5.5.2, apply with respect to such Client Money:

- (a) received in the form of cheque, or other payable order, until the Authorised Firm, or a Person or account controlled by the Authorised Firm, is in receipt of the proceeds of that cheque;
- (b) temporarily held by an Authorised Firm before forwarding to a Person nominated by the Client; or
- (c) in connection with a Delivery Versus Payment Transaction where:
 - (i) in respect of a Client purchase, Client Money from the Client will be due to the Authorised Firm within one day upon the fulfilment of a delivery obligation; or
 - (ii) in respect of a Client sale, Client Money will be due to the Client within one day following the Client's fulfilment of a delivery obligation.

A5.5.2 An Authorised Firm must pay Client Money of the type described in Rule A5.5.1(b) or (c) into a Client Account where it has not fulfilled its delivery or payment obligation within three days of receipt of the Money or Investments unless in the case of the type of Client Money referred to in Rule A5.5.1(c)(ii) it instead safeguards Client Investments at least equal to the value of such Client Money.

- A5.5.3** (1) An Authorised Firm must maintain adequate records of all cheques and payment orders received in accordance with Rule A5.5.1(a) including, in respect of each payment, the:
- (a) date of receipt;
 - (b) name of the Client for whom payment is to be credited; and
 - (c) date when the cheque or payment order was presented to the Authorised Firm's Third Party Agent.
- (2) The records must be kept for a minimum of six years.

A5.6 Appointment of a third party agent

- A5.6.1** (1) An Authorised Firm may only pay, or permit to be paid, Client Money to a Third Party Agent in accordance with Rule A5.7.1 where it has undertaken a prior assessment of the suitability of that agent and concluded on reasonable grounds that the Third Party Agent is suitable to hold that Client Money in a Client Account.
- (2) When assessing the suitability of the Third Party Agent, the Authorised Firm must ensure that the Third Party Agent will provide protections equivalent to the protections conferred by this appendix.
- (3) An Authorised Firm must have systems and controls in place to ensure that the Third Party Agent remains suitable.
- A5.6.2** An Authorised Firm must be able to demonstrate to the DFSA's satisfaction the grounds upon which the Authorised Firm considers the Third Party Agent to be suitable to hold that Client Money.

Guidance

When assessing the suitability of a Third Party Agent, an Authorised Firm should have regard to:

- a. its credit rating;
- b. its capital and financial resources in relation to the amount of Client Money held;
- c. the insolvency regime of the jurisdiction in which it is located;
- d. its regulatory status and history;
- e. its Group structure; and
- f. its use of agents and service providers.

A5.7 Payment of client money to a third party agent

- A5.7.1** (1) Subject to Rule A5.7.3, an Authorised Firm may only pass, or permit to be passed, a Segregated Client's Money to a Third Party Agent if:
- (a) the Client Money is to be used in respect of a Transaction or series of Transactions for that Client;
 - (b) the Client Money is to be used to meet an obligation of that Client; or
 - (c) the Third Party Agent is a Bank or a Regulated Financial Institution which is authorised to accept or take Deposits.
- (2) In respect of (1)(a) and (b), an Authorised Firm must not hold any excess Client Money with the Third Party Agent longer than necessary to effect a Transaction or satisfy the Client's obligation.

A5.7.2 When an Authorised Firm opens a Client Account with a Third Party Agent it must obtain, within a reasonable period, a written acknowledgement from the Third Party Agent stating that:

- (a) all Money standing to the credit of the account is held by the Authorised Firm as agent and that the Third Party Agent is not entitled to combine the account with any other account or to exercise any charge, mortgage, lien, right of set-off or counterclaim against Money in that account in respect of any sum owed to it on any other account of the Authorised Firm; and
- (b) the title of the account sufficiently distinguishes that account from any account containing Money that belongs to the Authorised Firm, and is in the form requested by the Authorised Firm.

Guidance

The DFSA would consider twenty days as being a reasonable period for an Authorised Firm to receive a written acknowledgement from the Third Party Agent.

A5.7.3 If the Third Party Agent does not provide the acknowledgement referred to in Rule A5.7.2 within a reasonable period, the Authorised Firm must refrain from making further deposits of Client Money with that Third Party Agent and withdraw any Client Money standing to the credit of that Client Account.

A5.8 Payment of client money from client accounts

A5.8.1 An Authorised Firm must have procedures for ensuring all withdrawals from a Client Account are authorised.

A5.8.2 Subject to Rule A5.8.3, a Segregated Client's Client Money must remain in a Client Account until it is:

- (a) due and payable to the Authorised Firm;

- (b) paid to the Client on whose behalf the Client Money is held;
- (c) paid in accordance with a Client instruction on whose behalf the Client Money is held;
- (d) required to meet the payment obligations of the Client on whose behalf the Client Money is held; or
- (e) paid out in circumstances that are otherwise authorised by the DFSA.

A5.8.3 Money paid out by way of cheque or other payable order under Rule A5.8.2 must remain in a Client Account until the cheque or payable order is presented to the Client's bank and cleared by the paying agent.

A5.8.4 An Authorised Firm must not use Client Money belonging of one Client to satisfy an obligation of another Client.

Guidance

The effect of Rule A5.8.4 is that an Authorised Firm would be required to deposit its own Money into a Client Account to remedy a shortfall arising from a client debit balance.

A5.8.5 An Authorised Firm must have a system for ensuring no off-setting or debit balances occur on Client Accounts.

A5.9 Client disclosure

A5.9.1 Before, or as soon as reasonably practicable after, an Authorised Firm receives Client Money belonging to a Segregated Client, it must disclose to the Client on whose behalf the Client Money is held:

- (a) the basis and any terms governing the way in which the Client Money will be held;
- (b) that the Client is subject to the protection conferred by the DFSA's Client Money Provisions and as a consequence:
 - (i) this Money will be held separate from Money belonging to the Authorised Firm; and
 - (ii) in the event of the Authorised Firm's insolvency, winding up or other Distribution Event stipulated by the DFSA, the Client's Money will be subject to the DFSA's Client Money Distribution Rules;
- (c) whether interest is payable to the Client and, if so, on what terms;
- (d) if applicable, that the Client Money may be held in a jurisdiction outside the DIFC and the market practices, insolvency and legal regime applicable in that jurisdiction may differ from the regime applicable in the DIFC;

- (e) if applicable, details about how any Client Money arising out of Islamic Financial Business are to be held;
- (f) if applicable, that the Authorised Firm holds or intends to hold the Client Money in a Client Account with a Third Party Agent which is in the same Group as the Authorised Firm; and
- (g) details of any rights which the Authorised Firm may have to realise Client Money held on behalf of the Client in satisfaction of a default by the Client or otherwise, and of any rights which the Authorised Firm may have to close out or liquidate contracts or positions in respect of any of the Client's Investments.

A5.10 Client reporting

A5.10.1 (1) In relation to a Client to whom the Client Money Provisions are applicable, an Authorised Firm must send a statement to the a Retail Client at least monthly or in the case of a Professional Client at other intervals as agreed in writing with the Professional Client.

- (2) The statement must include:
 - (a) the Client's total Client Money balances held by the Authorised Firm reported in the currency in which the Client Money is held, or the relevant exchange rate if not reported in the currency in which the Money is held;
 - (b) the amount, date and value of each credit and debit paid into and out of the account since the previous statement; and
 - (c) any interest earned and charged on the Client Money since the previous statement.
- (3) The statement sent to the Client must be prepared within 25 days of the statement date.

A5.11 Reconciliation

A5.11.1 (1) An Authorised Firm must maintain a system to ensure that accurate reconciliations of the Client Accounts are carried out at least every 25 days.

- (2) The reconciliation must include:
 - (a) a full list of individual Segregated Client credit ledger balances, as recorded by the Authorised Firm;
 - (b) a full list of individual Segregated Client debit ledger balances, as recorded by the Authorised Firm;

- (c) a full list of unpresented cheques and outstanding lodgements;
 - (d) a full list of Client Account cash book balances; and
 - (e) formal statements from Third Party Agents showing account balances as at the date of reconciliation.
- (3) An Authorised Firm must:
- (a) reconcile the individual credit ledger balances, Client Account cash book balances, and the Third Party Agent Client Account balances;
 - (b) check that the balance in the Client Accounts as at the close of business on the previous day was at least equal to the aggregate balance of individual credit ledger balances as at the close of business on the previous day; and
 - (c) ensure that all shortfalls, excess balances and unresolved differences, other than differences arising solely as a result of timing differences between the accounting systems of the Third Party Agent and the Authorised Firm, are investigated and, where applicable, corrective action taken as soon as possible.
- (4) An Authorised Firm must perform the reconciliations in (3) within 10 days of the date to which the reconciliation relates.

Guidance

When performing the reconciliations, an Authorised Firm should:

- a. include in the credit ledger balances:
 - i. unallocated Client Money;
 - ii. dividends received and interest earned and allocated;
 - iii. sale proceeds which have been received by the Authorised Firm and the Client has delivered the Investments or the Authorised Firm holds or controls the Investment; and
 - iv. Money paid by the Client in respect of a purchase where the Authorised Firm has not remitted the Money to the counterparty or delivered the Investment to the Client; and
- b. deduct from the credit ledger balances:
 - i. Money owed by the client in respect of unpaid purchases by or for the Client if delivery of those Investments has been made to the Client; and
 - ii. Money remitted to the Client in respect of sales transactions by or for the Client if the Client has not delivered the Investments.

A5.11.2 An Authorised Firm must ensure that the process of reconciliation does not give rise to a conflict of interest.

Guidance

When performing reconciliations, an Authorised Firm should maintain a clear separation of duties to ensure that an employee with responsibility for operating Client Accounts, or an employee that has the authority to make payments, does not perform the reconciliations under Rule A5.11.1

- A5.11.3** (1) Reconciliation performed in accordance with Rule A5.11.1 must be reviewed by a member of the Authorised Firm who has adequate seniority.
- (2) The individual referred to in (1) must provide a written statement confirming the reconciliation has been undertaken in accordance with the requirements of this section.

A5.11.4 The Authorised Firm must notify the DFSA where there has been a material discrepancy with the reconciliation which has not been rectified.

Guidance

A material discrepancy includes discrepancies which have the cumulative effect of being material, such as longstanding discrepancies.

A5.12 Auditor's reporting requirements

Guidance

In accordance with GEN chapter 8, an Authorised Firm which holds Client Money for Segregated Clients must arrange for a Client Money Auditor's Report to be submitted to the DFSA on an annual basis.

A5.13 Client money distribution rules

A5.13.1 This section is referred to as the Client Money Distribution Rules and to the extent that these Rules are inconsistent with part 4.13 of the Insolvency Regulations, these Rules will prevail.

A5.13.2 Following a Distribution Event, the Authorised Firm must distribute Money in the following order of priorities:

- (a) firstly, in relation to Client Money held in a Client Account on behalf of Segregated Clients, claims relating to that Money must be paid to each Segregated Client in full or, where insufficient funds are held in a Client Account, proportionately, in accordance with each Segregated Client's valid claim over that Money;
- (b) secondly, where the amount of Client Money in a Client Account is insufficient to satisfy the claims of Segregated Clients in respect of that Money, or not being immediately available to satisfy such

- claims, all other Money held by the Authorised Firm must be used to satisfy any outstanding amounts remaining payable to Segregated Clients but not satisfied from the application of (a) above;
- (c) thirdly, upon resolution of claims in relation to Segregated Clients, any Money remaining with the Authorised Firm must be paid to each Client in full or, where insufficient funds are held by the Authorised Firm, proportionately, in accordance with each Client's valid claim over that Money; and
 - (d) fourthly, upon satisfaction of all claims in (a), (b) and (c) above, in the event of:
 - (i) the appointment of a liquidator, receiver or administrator, or trustee in bankruptcy over the Authorised Firm, payment must be made accordance with the Insolvency Law 2004; or
 - (ii) all other Distribution Events, payment must be made in accordance with the direction of the DFSA.

Guidance

A Segregated Client would not have a valid claim over Client Money held in a Client Account if that Client Account was not established to hold Client Money for that Client.

A5.13.3 Following a Distribution Event, an Authorised Firm must sell all Collateral and use the proceeds of the sale to satisfy claims made in accordance with Rule A5.13.2

A5.14 Failure to comply with this appendix

A5.14.1 An Authorised Firm which becomes aware that it does not comply with any Rule in this appendix must, within one day, give notice of that fact to the DFSA.

APP6 SAFE CUSTODY PROVISIONS

A6.1 Application

A6.1.1 ~~In accordance with Rule 6.13.3, this~~ This appendix applies to an Authorised Firm in accordance with Rule 6.13.3, which Provides Custody or Arranges Custody

A6.2 General requirements

A6.2.1 The provisions of this appendix are referred to as the Safe Custody Provisions.

A6.2.2 An Authorised Firm ~~which Provides Custody or Arranges Custody~~ must:

- (a) comply with the Safe Custody Provisions; and
- (b) have adequate systems and controls in place to be able to evidence compliance with the Safe Custody Provisions.

A6.3 Recording, registration and holding requirements

A6.3.1 An Authorised Firm which Provides Custody or holds or controls Client Investments must ensure that Safe Custody Investments are recorded, registered and held in an appropriate manner to safeguard and control such property.

A6.3.2 Subject to Rule A6.4.1, an Authorised Firm which Provides Custody or holds or controls Client Investments must record, register and hold Safe Custody Investments separately from its own Investments.

A6.4 Client accounts in relation to Client Investments

A6.4.1 An Authorised Firm which Provides Custody or holds or controls Client Investments must register or record all Safe Custody Investments in the legal title of:

- (a) a Client Account; or
- (b) the Authorised Firm where, due to the nature of the law or market practice, it is not feasible to do otherwise.

- A6.4.2** A Client Account in relation to Client Investments is an account which:
- (a) is held with a Third Party Agent or by an Authorised Firm which is authorised under its Licence to Provide Custody;
 - (b) is established to hold Client Assets;
 - (c) when held by a Third Party Agent, is maintained in the name of;
 - (i) if a Domestic Firm ~~incorporated in the DIFC~~, the Authorised Firm; or
 - (ii) if not a Domestic Firm ~~the Authorised Firm is not incorporated in the DIFC~~, a Nominee Company controlled by the Authorised Firm; and
 - (d) includes the words 'Client Account' in its title.

- A6.4.3**
- (1) An Authorised Firm must maintain a master list of all Client Accounts.
 - (2) The master list must detail:
 - (a) the name of the account;
 - (b) the account number;
 - (c) the location of the account;
 - (d) whether the account is currently open or closed; and
 - (e) the date of opening or closure.
 - (3) The details of the master list must be documented and maintained for a minimum period of six years following the closure of an account.

Guidance

- 1. An Authorised Firm may record, register or hold a Client's Investment in a Client Account solely for that Client. Alternatively, an Authorised Firm may choose to pool that Client's Investment in a Client Account containing Investments of more than one Client.
- 2. The purpose of recording, registering or holding Investments in a Client Account is to ensure that Investments belonging to Clients are readily identifiable from Investments belonging to the Authorised Firm such that, following a Distribution Event, any subsequent distribution of Investments may be made in proportion to each Client's valid claim over those Investments.
- 3. Following a Distribution Event, a Client ~~will~~ may not have a valid claim over Investments registered, recorded or held in a Client Account if that Client Account was not established to register, record or hold Investments for that Client or pool of Clients.

A6.4.4 An Authorised Firm ~~which Provides Custody~~ must not use a Client's Safe Custody Investment for its own purpose or that of another Person without that Client's prior written permission.

A6.4.5 An Authorised Firm which intends to use a Client's Safe Custody Investments for its own purpose or that of another Person, must have systems and controls in place to ensure that:

- (a) it obtains that Client's prior written permission;
- (b) adequate records are maintained to protect Safe Custody Investments which are applied as collateral or used for stock lending activities;
- (c) the equivalent assets are returned to the Client Account of the Client; and
- (d) the Client is not disadvantaged by the use of his Safe Custody Investments.

A6.5 Holding or arranging custody with third party agents

A6.5.1 (1) Before an Authorised Firm holds a Safe Custody Investment with a Third Party Agent or Arranges Custody through a Third Party Agent, it must undertake an assessment of that Third Party Agent and have concluded on reasonable grounds that the Third Party Agent is suitable to hold those Safe Custody Investments.

(2) An Authorised Firm must have systems and controls in place to ensure that the Third Party Agent remains suitable.

(3) When assessing the suitability of the Third Party Agent, the Authorised Firm must ensure that the Third Party Agent will provide protections equivalent to the protections conferred in this appendix.

A6.5.2 An Authorised Firm must be able to demonstrate to the DFSA's satisfaction the grounds upon which the Authorised Firm considers the Third Party Agent to be suitable to hold Safe Custody Investments.

Guidance

When assessing the suitability of a Third Party Agent, an Authorised Firm should have regard to:

- a. its credit rating;
- b. its capital and financial resources in relation to the amount of Safe Custody Investments held;
- c. the insolvency regime of the jurisdiction in which it is located;
- d. its arrangements for holding the Investments;
- e. its regulatory status, expertise, reputation and history;

- f. its Group structure;
- g. its use of agents and service providers; and
- h. any other activities of the agent.

A6.6 Safe custody agreements with third party agents

A6.6.1 Before an Authorised Firm ~~Providing Custody~~ passes, or permits to be passed, Safe Custody Investments to a Third Party Agent it must have procured a written acknowledgement from the Third Party Agent stating:

- (a) that the title of the account sufficiently distinguishes that account from any account containing Investments belonging to the Authorised Firm, and is in the form requested by the Authorised Firm;
- (b) that the Client Investment will only be credited and withdrawn in accordance with the instructions of the Authorised Firm;
- (c) that the Third Party Agent will hold Client Investments separately from assets belonging to the Third Party Agent;
- (d) the arrangements for recording and registering Client Investments, claiming and receiving dividends and other entitlements and interest and the giving and receiving of instructions;
- (e) that the Third Party Agent will deliver a statement to the Authorised Firm (including the frequency of such statement), which details the Client Investments deposited to the account;
- (f) that all Investments standing to the credit of the account are held by the Authorised Firm as agent and that the Third Party Agent is not entitled to combine the account with any other account or to exercise any charge, mortgage, lien, right of set-off or counterclaim against Investments in that account in respect of any sum owed to it on any other account of the Authorised Firm; and
- (g) ~~The~~ the extent of liability of the Third Party Agent in the event of default.

- A6.6.2**
- (1) An Authorised Firm must maintain records of all Safe Custody Agreements and any instructions given by the Authorised Firm to the Third Party Agent under the terms of the agreement.
 - (2) The records must be maintained for at least of six years.

A6.7 Client disclosure

- A6.7.1** (1) Before an Authorised Firm Arranges Custody for a Client it must disclose to that Client, if applicable, that the Client's Safe Custody Investments may be held in a jurisdiction outside the DIFC and the market practices, insolvency and legal regime applicable in that jurisdiction may differ from the regime applicable in the DIFC.
- (2) Before an Authorised Firm Provides Custody for a Client it must disclose to the Client on whose behalf the Safe Custody Investments will be held:
- (a) a statement that the Client is subject to the protections conferred by the Safe Custody Provisions;
 - (b) the arrangements for recording and registering Safe Custody Investments, claiming and receiving dividends and other entitlements and interest and the giving and receiving instructions relating to those Safe Custody Investments;
 - (c) the obligations the Authorised Firm will have to the Client in relation to exercising rights on behalf of the Client;
 - (d) the basis and any terms governing the way in which Safe Custody Investments will be held, including any rights which the Authorised Firm may have to realise Safe Custody Investments held on behalf of the Client in satisfaction of a default by the Client;
 - (e) the method and frequency upon which the Authorised Firm will report to the Client in relation to his Safe Custody Investments;
 - (f) if applicable, a statement that the Authorised Firm intends to mix Safe Custody Investments with those of other Clients;
 - (g) if applicable, a statement that the Client's Safe Custody Investments may be held in a jurisdiction outside the DIFC and the market practices, insolvency and legal regime applicable in that jurisdiction may differ from the regime applicable in the DIFC;
 - (h) if applicable, a statement that the Authorised Firm holds or intends to hold Safe Custody Investments in a Client Account with a Third Party Agent which is in the same Group as the Authorised Firm; and
 - (i) the extent of the Authorised Firm's liability in the event of default by a Third Party Agent.

A6.8 Client reporting

- A6.8.1** (1) An Authorised Firm which Provides Custody or which holds or controls Client Investments for a Client must send a statement to ~~that~~ a Retail Client at least every six months or in the case of a Professional Client at other intervals as agreed in writing with the Professional Client.
- (2) The statement must include:
- (a) a list of that Client's Safe Custody Investments as at the date of reporting;
 - (b) a list of that Client's Collateral and the market value of that Collateral as at the date of reporting; and
 - (c) details of any Client Money held by the Authorised Firm as at the date of reporting.
- (3) The statement sent to the Client must be prepared within 25 business days of the statement date.

A6.9 Reconciliation

- A6.9.1** An Authorised Firm ~~which Provides Custody~~ must:
- (a) at least every 25 business days, reconcile its records of Client Accounts held with Third Party Agents with monthly statements received from those Third Party Agents;
 - (b) at least every six months, count all Safe Custody Investments physically held by the Authorised Firm, or its Nominee Company, and reconcile the result of that count to the records of the Authorised Firm; and
 - (c) at least every six months, reconcile individual Client ledger balances with the Authorised Firm's records of Safe Custody Investment balances held in Client Accounts.
- A6.9.2** An Authorised Firm must ensure that the process of reconciliation does not give rise to a conflict of interest.

Guidance

An Authorised firm should maintain a clear separation of duties to ensure that an employee with responsibility for operating Client Accounts, or an employee that has authority over Safe Custody Investments, should not perform the reconciliations under Rule A6.9.1.

- A6.9.3** (1) Reconciliation performed in accordance with section A6.9 must be reviewed by a member of the Authorised Firm who has adequate seniority.
- (2) The ~~person~~ individual referred to in (1) must provide a written statement confirming the reconciliation has been undertaken in accordance with the requirements of this section.

A6.9.4 The Authorised Firm must notify the DFSA where there have been material discrepancies with the reconciliation which have not been rectified.

Guidance

A material discrepancy includes discrepancies which have the cumulative effect of being material, such as longstanding discrepancies.

A6.10 Auditor's reporting requirements

Guidance

In accordance with GEN chapter 8, an Authorised Firm to which Provides Custody ~~this appendix applies~~ must arrange for a Safe Custody Auditor's Report to be submitted to the DFSA on an annual basis.