FEEDBACK STATEMENT ON CP160 UPDATES TO THE CLIENT ASSETS REGIME

14 MARCH 2025

Why are we issuing this Feedback Statement?

From time to time, the DFSA issues Feedback Statements to explain the conclusions we have reached following a consultation process. We do this, in particular, where we think it is helpful to:

- share the overview of responses we received to a particular consultation paper;
- illustrate the factors that were considered in reaching the conclusions;
- explain any changes made in the final rules compared to the proposals in the consultation paper; and
- describe why some suggestions were not taken on board in the final rules.

The overall purpose of the Feedback Statement is to assist with regulatory understanding and expectations, and to provide transparency.

Who should read this Statement?

This Feedback Statement is likely to be of interest to:

- Authorised Firms;
- Registered Auditors;
- Applicants to become any of the above; and
- Professional advisers to Authorised Firms.

DFSA response to public comments on CP160 – Updates to the Client Assets Regime

I BACKGROUND

1. This paper explains how we have considered the public comments received on the proposed changes to the DFSA's Client Assets Regime out in Consultation Paper No. 160[1] ("CP160").

2. On 6 August 2024, CP160 was released for public comments for a period of 75 days. We extend our thanks to all those who contributed to the consultation process.

3. In late February 2025, the DFSA Board considered the consultation responses and approved the making of the updated Client Asset rules (set out in the revised GEN, COB, CIR, GLO, AUD and MKT modules).

4. The revised rules are published on the same day as this Feedback Statement and will come into force on 1 January 2026.

II PUBLIC COMMENTS

Investment management of Funds

5. Under the current Client Asset rules[2], Money that falls under the definition of Fund Property[3] does not constitute Client Money. As a result, from the perspective of a DFSA Authorised Firm that is a Fund Manager, the Money falls under the Fund Property protection rules in the Collective Investment Law[4] (CIL) and the Collective Investment Rules (CIR), rather than the Client Asset rules.

6. The current rules do not extend to the other two elements of the definition of Client Assets (i.e. Investments and Crypto Tokens). Therefore, in CP160, we proposed to avoid duplication and clarify that assets constituting Fund Property do not fall within the definition of Client Assets.[5]

7. The practical implication of this proposal is that a DFSA Authorised Firm acting in the capacity of an investment manager, which is engaged exclusively in the activity of managing funds under a delegation would no longer be subject to the Client Assets rules (because the assets would be Fund Property) and thus would not be required to have the Client Asset endorsement.

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[1] CP160.
[2] COB rule 6.12.1(f).
[3] The GLO module defines fund property as "*The property held for or within a Fund*". The Collective Investment Law[3] says that "*A Fund is either a Domestic or a Foreign Fund*".
[4] Collective Investment Law No. 2 of 2010.
[5] COB rule 6.13.1 and COB rule 6.13.1A.

Fund Property of Foreign Funds

8. Some commentators sought confirmation as to whether the proposal also includes the Fund Property of a Foreign Fund[6] managed under a delegation by a DFSA Authorised Firm acting in the capacity of an investment manager. We confirm that the proposed change does include the Fund Property of a Foreign Fund. In practice, this means that the Fund Property of the Foreign Fund is not subject to the DFSA's Client Asset rules or the Fund Property protections in the CIL and CIR. This is on the basis that the property of the Foreign Fund would be subject to legal protections applicable in the jurisdiction of the fund or the fund manager, as the case may be.

9. We would not expect to see any instances of client facing materials containing inaccurate or misleading statements indicating that the protections under the DFSA's Client Assets regime apply, when in fact they do not.

Sub-delegation of investment management

10. Comments were received asking for clarification as to whether the same approach (i.e. that the Client Assets rules are no longer relevant) would also apply in the case of a DFSA authorised investment manager receiving a sub delegation from another investment manager. We confirm that the same approach applies regardless of how many layers of delegation there are.

Client Assets crisis preparedness pack

11. In CP160, we proposed the introduction of a new requirement that Authorised Firms compile and maintain a pack of documents, referred to as a Client Assets crisis preparedness pack (Pack), which should include vital existing information for the identification of Client Assets.[7] The Pack is designed to assist relevant parties such as insolvency practitioners, accountants, lawyers and regulators with swift identification, retrieval and return of Client Assets in crisis situations.

Scope of application

12. Some commentators sought clarification as to the scope of application of the Pack for Authorised Firms that only control Client Assets under COB rule 6.11.4(d). In such circumstances the Client Assets are held in an account in the Client's own name and the Client has access to its own accounts and the assets therein. In this scenario, there should be no issue with the return of Client Assets. Therefore, we confirm that the Pack is only required for Authorised Firms that "hold" Client Assets under COB rule 6.11.4(a-c). This is clarified in COB rule 6.11.2(4).

[6] CIL Article 13(3) provides that a Foreign Fund is a Fund that is not a Domestic Fund (DIFC based) or an External Fund (established outside the DIFC but managed by a DFSA authorised Fund Manager). A foreign fund is therefore a fund that is not based in the DIFC and is not managed by a DFSA authorised Fund Manager.
[7] COB section 6.14.

Updates to the Pack

13. Regarding the frequency of the Pack updates and the type of changes that we expect to trigger an update, we wish to clarify the following:
    a) While COB rule 6.14.3(1) provides that the Pack needs to be kept 'up to date' on an ongoing basis, COB rule 6.14.3(2) provides for a timeframe of a maximum of five business days to update the Pack after a change occurs.
    b) The proposed draft rule in COB rule 6.14.3(2) originally stated that the Pack should be updated "*if any change of circumstances has the effect of making inaccurate or out of date, in any material respect, the content of the Client Assets Pack*". However, following the consultation, we have concluded that for the Pack to be useful to relevant parties (particularly in the event of a crisis), it is vital that all elements of the Pack are kept up to date and inaccuracies corrected. Therefore, we have removed the reference to "*in any material effect*" from COB rule 6.14.3(2).

Integration within business continuity and disaster recovery plans

14. Some commentators asked for guidance on whether the Pack can be integrated into existing business continuity and disaster recovery plans[8] to avoid duplication and ensure smooth implementation. We confirm that if Authorised Firms already possess the information required to be included in the Pack, and provided that all of the required Client Asset information listed in COB rule 6.14.2 is contained in their existing business continuity and disaster recovery plans, this will suffice to satisfy this obligation.

Client Assets Auditor's Report[9]

Material discrepancies in reconciliations

15. Currently, the Client Assets Auditor's Reports must state whether there have been any material discrepancies in Client Asset reconciliations.[10] To facilitate more targeted supervisory engagement, in CP160, we proposed that the Auditor should also state whether the Authorised Firm has taken appropriate action to rectify any material discrepancies identified.

16. Commentators expressed concerns with the proposal to require Auditors to make a judgment on whether the Authorised Firm has taken appropriate action to rectify any material discrepancies identified by the Auditors. We acknowledge that it would require a subjective assessment and goes beyond the scope of ISRS 4400[11] which focuses mainly on "Agreed-Upon Procedures Engagements".

[8] Required by GEN rule 5.3.23.
[9] "Client Assets Auditor's Report" is a collective term for the purposes of the Feedback Statement. It refers to the Client Money Auditor's Report, the Safe Custody Investment Auditor's Report and the Safe Custody Crypto Tokens Auditor's Report.
[10] AUD rule A2.2.1(b)(vii) and AUD rule A4.1.1(b)(iii).
[11] https://www.ifac.org/_flysystem/azure-private/publications/files/ISRS-4400-Revised-Agreed-Upon-Procedures-final.pdf

17. Consequently, we have decided not to follow through with this proposal and to maintain the current requirement, i.e. where the Auditor only takes note of the factual situation of whether it observed any material discrepancies in Client Asset reconciliations. We will continue to follow-up with Authorised Firms through our usual supervisory engagement and review of Auditor's Reports to ensure that any material discrepancies identified in reconciliations have been promptly rectified.

Report to DFSA on Auditor's findings

Scope of report to DFSA on Auditor's findings

18. To facilitate more targeted supervisory engagement, in CP160 we proposed a requirement that an Authorised Firm report to the DFSA on the remedial steps being taken (or that have been taken) to address the findings of material non-compliance noted in the Client Assets Audit Reports.[12]

19. In light of the submissions that in their engagements under ISRS 4400 Auditors do not make judgments on the materiality of non-compliance and that they only report findings of fact, we have removed the reference to 'materiality'. As a result, Authorised Firms should ensure that remedial actions in respect of all of the Auditor's findings are included in the report to the DFSA.

Deadline to submit report to DFSA on Auditor's findings

20. In CP160, we proposed that the Authorised Firms should send the report on the Auditor's findings to the DFSA within 30 days of the submission of the Client Assets Auditor's Report. Some commentators called for a longer period to submit the report to the DFSA. We believe it was likely based on a misunderstanding of the nature of the report and an assumption that the report would require a notification that the non-compliance findings have already been fully resolved within the 30 day period.

21. Our expectation is that Authorised Firms should report to the DFSA within 30 days on any steps they:
    a) are taking to rectify findings of non-compliance; or
    b) have already taken. This would, for example, be the case if the non-compliance has already been rectified.

    The DFSA does not expect rectification to have been completed within the 30 days. Our expectations on the time within which rectification is completed will be a separate matter and will depend on the nature, size and complexity of the matter. We have added guidance to COB rules A5.12 and A6.10 to clarify this further.

[12] COB rule A5.12 and COB rule A6.10.

Third Party Agent suitability assessment

22. In CP160 we proposed to change the matters to be considered in the Third Party Agent (TPA) suitability assessment from guidance to rules.[13] While some respondents agreed that this could lead to consistent practices, they also expressed concerns that the unavailability of some information could limit their ability to consider all the matters in the assessment.

23. In that regard, we wish to clarify that the focus of this requirement is on Authorised Firms undertaking proper consideration of the matters listed for the TPA suitability assessment. We have also added guidance[14] that explains that Authorised Firms should document and maintain records of the TPA suitability assessment and how the matters have been considered. Please note that while there is no express obligation that Authorised Firms meet each and every one of the matters, the protection of Client Assets is a cornerstone of the DFSA's regime and it is expected that Authorised Firms will undertake a proper and thorough assessment when selecting TPAs. Authorised Firms should be prepared to explain to the DFSA, on request, where a particular matter has not been assessed or deemed not applicable.

Creditworthiness assessment

24. In response to the comments requesting more clarity on what should be considered as part of an assessment of a TPA's creditworthiness[15], we have added guidance to assist Authorised Firms in this regard.[16]

Diversification

25. In relation to the proposed consideration of diversification of Client Money across TPAs as part of the suitability assessment[17], some commentators expressed concerns about the operational complexity of such an arrangement, particularly for smaller firms. Others inquired about the recommended rate of split of Client Money placements across TPAs.

26. In this regard, we would like to clarify that the rules are deliberately principle-based and do not prescribe whether and how the diversification should be achieved. Firms will be best placed to exercise this judgement; such analysis will be circumstantial, and firms should consider (amongst other things) the risks stemming from concentrating all Client Money placements with one TPA only, or any particular TPA, and whether any (and what) mitigation measures are necessary.

[13] COB rule A5.6 and COB rule A6.5.
[14] Guidance item 3 to COB rule A5.6 and guidance item 2 to COB rule A6.5.
[15] COB A5.6.1(2)(b) and COB A6.5.3(b).
[16] Guidance item 1 to COB rule A5.6.2 and guidance item 1 to COB rule A6.5.4
[17] COB rule A5.6.2(h).

Client disclosures

Disclosure on insolvency regime in TPA's jurisdiction

27. In CP160, we proposed that Authorised Firms let Clients know that, upon request, they can obtain information about the outcome of the assessment of the insolvency regime in the TPA's jurisdiction. The Authorised Firm should already have such information at its disposal as it forms part of the TPA suitability assessment.

28. The submissions questioned the usefulness of the proposed disclosure. Upon reflection, we acknowledge that disclosing the outcome of the suitability assessment would have limited value.

29. Instead, we propose to make the disclosure more relevant for the Client by shifting the focus to the relevant aspects of the insolvency regime in the TPA's jurisdiction.[18] By "relevant aspects" we mean the parts of the insolvency regime in the TPA's jurisdiction which would be relevant to the Client's understanding of how its assets held with the TPA would be treated in the event that the TPA were to enter into insolvency. This would also include, in the case of Client Money, information on the existence and scope of a depositor guarantee scheme or depositor preference in the TPA's jurisdiction.

Client Asset reconciliations

Frequency

30. Currently, Authorised Firms are required to reconcile records of Client Investments against the statements received from the TPA at least every 25 business days and perform Client Money reconciliations every 25 calendar days.

31. In CP160, we proposed that the reconciliation in respect of Client Investments should be performed within at least five business days of receipt of the statement from the TPA. We did not suggest any changes to the frequency of Client Money reconciliations apart from adding guidance indicating factors that should induce Authorised Firms to consider performing more frequent reconciliations.

32. The comments we received expressed concern that the proposed timing to perform the reconciliation of Client Investments with the TPA statement was too short. Additionally, commentators asked for the requirement related to the frequency of reconciliations in respect of Client Investments and Client Money (25 calendar days vs. 25 business days respectively) to be aligned.

[18] COB rule A5.9.1(f), COB rule A6.7.1(b) and COB rule A6.7.1(2)(h).

33. In response to these comments, we have decided to update the reconciliation requirements for both Client Investments and Client Money so that they are to be carried out at least monthly.[19]

Client Investments reporting

Professional Clients

34. In CP160, we proposed to change the required frequency of reporting on Client Investments to Professional Clients from intervals agreed in writing (between the Authorised Firm and the Professional Client) to monthly.

35. Commentators suggested that many Professional Clients tend to opt out of receiving Client Investment reports and instead rely solely on a real-time online access to verify their accounts. In light of these comments and to avoid unnecessary regulatory burden, we have decided not to follow through with this proposal and to maintain the current requirement.[20]

Transition period

36. While in CP160, we proposed a three month transition period in respect of the obligation to compile a Client Assets crisis preparedness pack, after considering the comments calling for a longer period to adapt their processes to all the new rules, we have decided to grant a longer transition period for all the new rules. As a result, the rules are published at the same time as this Feedback Statement and will become effective as of 1 January 2026.

III NEXT STEPS

37. The updated rules on Client Assets will come into force on **1 January 2026**, allowing Authorised Firms and Registered Auditors sufficient time to adopt the updated requirements. Authorised Firms and Registered Auditors should consider the updated rules in good time to ensure that they are able to comply as of the relevant date.

[19] COB rule A5.11.1(1) and COB rule A6.9.1(a).
[20] COB rule A6.8.1(1).