GOVERNANCE | RISK | COMPLIANCE

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Regulatory Update

Middle East Edition

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1.0 DFSA LATEST DEVELOPMENTS

1.1 Updates to the DFSA Regulatory Policy and Process Module

A new chapter has been added to the DFSA Regulatory Policy and Process (RPP) Module and came into effect on 14th July 2015. The newly added Chapter 10 of the RPP Module incorporates the DFSA's new "Naming Policy", which sets out the DFSA's policy on the names that Applicants, Authorised Firms, Funds and other entities established in the DIFC should use.

The policy aims to ensure that entities operating in or from the DIFC use names that are fair and clear so as not to mislead consumers and applies to any entity in the DIFC that uses or proposes to use in its business name or trading name:

(a) the word "bank" or any of its derivatives;
(b) the word "insurer" or any of its derivatives;
(c) the word "trust" or any of its derivatives;
(d) any other words connected to financial services;
(e) any other words which suggest that it is authorised to carry on a Financial Service; and
(f) any other words that are misleading in light of its actual business activities.

The DFSA has considered and adopted international best practice in formulating this policy. In particular the DFSA has considered the international standards promulgated by the Basel Committee on Banking Supervision in its Core Principles for Effective Banking Supervision. These principles require financial services regulators to control the use of specific words related to the conduct of banking business.

Following the release of the updated RPP Module, the DFSA sent a "Dear SEO Letter" to all Authorised Firms, advising that they should consider if it affects the name of their firm. If it does or could, it is recommended firms contact the DFSA to confirm that the firm needs a name change. The DFSA will then work with the firm to set out a timetable for transitioning to an agreed new name. The DFSA state that they will generally look at substance over form when considering requests to use a particular name and generally allow a six month period to transition to a new name. However, the DFSA may exceptionally allow a longer period if a firm can give a compelling reason to do so.

Additionally, the DFSA will shortly undertake its own review of authorised firms' names to identify if any firms are currently using a name which is contrary to the naming policy.

1.2 Arqaam Capital Limited Resolves Compliance Deficiencies with the DFSA

On 29th July 2015, The DFSA announced that it had accepted an Enforceable Undertaking (EU) from Arqaam Capital Limited (Arqaam). Arqaam also agreed to pay a financial penalty of USD 50,000.

The EU resulted from an investigation by the DFSA into Arqaam's AML systems and controls, customer AML risk assessments and CDD practices. The investigation followed a routine DFSA Risk Assessment in which deficiencies were identified, some of which involved the firm's client files. Upon review of the client files it was discovered that:

- There was a lack of any evidence that Arqaam was seeking to treat the customer as a Prescribed Low Risk Customer (as Arqaam claimed) or other evidence to justify a low risk rating;
- Client files did not contain sufficient evidence or explanation for the client AML risk ratings;
- Arqaam did not identify the ultimate beneficial owners of the customers;
- Client files contained expired identification documentation;
- Arqaam did not identify the directors of corporate entity clients;
- Arqaam did not adequately verify the customer's source of wealth; and
- Arqaam did not adequately verify the customer's source of funds.

Although no specific contraventions of DIFC/DFSA laws and regulations were cited in the EU, the DFSA were concerned that Arqaam may not have been in compliance with 2 of its 12 Core Principles as well as with elements of the DFSA AML Module. As a result, the DFSA requires Arqaam to implement and maintain effective AML systems and controls that comply with the DFSA's laws and regulations.

The DFSA acknowledged that Arqaam had fully co-operated throughout the investigation and sought an early amicable resolution, including the offer to appoint an independent AML expert and undertake remedial action.

The Terms and Conditions of the EU state that Arqaam will, within 45 days from the date of the EU, appoint a suitably qualified firm to assist Arqaam in carrying out remedial action on Arqaam's AML systems and controls. The independent expert and the terms of engagement must be approved by the DFSA. Within 30 days of appointing an independent expert, Arqaam together with the engaged firm, must submit a remediation plan to the DFSA for their approval. Once a remediation plan has been agreed, Arqaam will implement all of the tasks no later than six months from the date the plan was agreed by the DFSA.

Throughout the implementation of the remediation plan, the independent expert will monitor progress and ensure the plan is fully implemented and operating effectively. At the end of the six month period, the independent expert must file an assessment to the DFSA which confirms whether all action points within the remediation plan have been implemented effectively and are complete.

Further information
If you would like to discuss these latest developments in more detail, please contact:
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2.0 MIDDLE EAST REGULATORY UPDATES

2.1 ADGM Publishes Draft Regulations

Abu Dhabi Global Market (ADGM) has published its proposed financial services rules and regulations in draft form for public consultation purposes. The financial free zone said the regulation underscored its aim to provide a "well-regulated and internationally recognised platform to develop and support a vibrant financial services industry".

The foundation of the civil and commercial law in ADGM is provided by the Application of English Law Regulations, which makes English common law (including the rules and principles of equity) directly applicable in ADGM. In addition, a wide ranging set of English statutes on civil matters are also made applicable in ADGM. The direct application of English common law makes ADGM the first jurisdiction in the Middle East to adopt a similar approach to that of Singapore and Hong Kong.

The ADGM financial services regime is broadly modeled on the UK's financial services framework. There are also noticeable similarities to the DFSA's regulatory framework. For example, the DFSA's client classification regime has been replicated in the ADGM's draft COB Module.

A difference between the ADGM and DFSA frameworks is the ADGM's use of a The Financial Services and Markets Regulations (FSMR) which establishes the legislative and regulatory framework for financial services in ADGM. The FSMR has been broadly modeled on the UK' Financial Services and Markets Act 2000 and other related legislation. It is within the FSMR where financial services and their definitions are outlined. While the financial services that can be offered from the ADGM are the same as those set by the DFSA, the FSMR provides more clarity through detailed definitions for each financial service compared to the brief definitions set by the DFSA in the DFSA's GEN Module.

The ADGM is considering providing some form of exemption for entities in ADGM currently carrying on financial services business and already licensed by UAE authorities from the ADGM licensing and authorisation requirements for a period, subject to extension by the Regulator.

The consultation papers are available at ADGM's website (www.adgm.com) and the public consultation period will end on 11th August 2015.

2.2 Remaining Worries Over Iran's Nuclear Programme

After years of pressure, sanctions, coercion and tough negotiations that sought to ensure the peaceful nature of Iran's nuclear programme, Iran and the P5+1 (United States, Britain, France, Russia, China plus Germany) have finally reached an agreement. The agreement, formally called 'The Joint Comprehensive Plan of Action' (JCPA), will see the sanctions placed on the Islamic Republic of Iran lifted in exchange for Iran abandoning the military component of its nuclear programme.

The agreement also stipulates an immediate return of sanctions on Iran in the event of non-compliance. The lifting of the sanctions shall come into force only after confirmation by the International Atomic Energy Agency (IAEA), that Iran has fulfilled its obligations.

As far as the IAEA inspections are concerned, Iran has agreed to sign the additional protocol of the Nuclear Non-Proliferation Treaty (NPT). In line with the agreement, Iran will have 14 days during which it can respond to an IAEA request to visit any facility in the country. Should Iran deny a request to visit a specific site, the issue will be referred to an IAEA joint committee formed from seven parties, the P5+1 and the European Union. This committee will have seven days to decide on specific matters.

2.3 FATCA Guidance Notes Now Available Online

As part of the 2014 agreement signed between the UAE and USA to implement the Foreign Account Tax Compliance Act (FATCA) in the UAE, the Ministry of Finance (MoF) has announced that the UAE FATCA Guidance Notes along with a Registration Form for entities to access the FATCA reporting portal are now available on the Ministry's website.

The Guidance Notes provide a detailed explanation of the Foreign Account Tax Compliance Act (FATCA) and the terms and conditions for relevant financial institutions identified in the agreement and operating in the UAE banking, insurance and financial services sectors. The document also includes guidelines for submitting financial reports according to FATCA standards, the UAE's framework and legislation as well as updates on the laws issued by the US Treasury Department.

All relevant financial institutions and entities identified within the agreement are required to register on the portal using the Registration Form included in the Guidance Notes, which will be provided by their licensed authorities, including the UAE Central Bank, Securities and Commodities Authority, Insurance Authority, and Dubai International Financial Centre.

2.4 Insurance Companies Seek Improved Risk Management Framework

A significantly large number of insurance companies from the UAE and Saudi Arabia are seeking to enhance their risk management framework in the context of regulatory requirements. According to The Mena Insurance Enterprise Risk Management (ERM) survey conducted by Ernst & Young and Munich RE, 41 per cent of insurance companies in Saudi Arabia and the UAE believe there is a need to improve their overall risk management framework. The survey identifies risk management challenges that insurance companies face and takes a view on the evolving risk governance practices.

There is also increased pressure from regulators and rating agencies, as well as competitors. "Insurance companies that move first to an improved model of managing their business and their capital resources economically, will see the maximum benefit," said Andreas Pollmann, client executive, Mena, Munich RE.

Even if some of the insurers have established an enterprise-wide risk appetite, many have not been able to effectively lead this to the operational level and embed it into their decision making or insurance value chain. Saudi insurers rated "business taking ownership of risk" as the top challenge to strengthening the risk culture, whereas UAE insurers rated "lack of a strong regulatory regime and competitive pressures" as the top challenges for them.

A number of these challenges are expected to be addressed following the recently issued regulatory guidelines from the UAE Insurance Authority.

Further information
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3.0 INTERNATIONAL DEVELOPMENTS

3.1 New York Regulator Scrutinises Consultancy Firm's Work Undertaken for Standard Chartered

New York's Department of Financial Services (DFS) is probing whether Promontory altered a 2011 report to regulators about the bank's Iranian transactions to water down alleged sanction violations.

Promontory is a well established strategy, risk management, and regulatory compliance consulting firm focusing primarily on the financial services industry. With a presence in North America, Europe, Asia, Australia, and the Middle East, the firm boasts of having clients in more than 50 countries on six continents.

The move by the DFS is a threat to the reputation of Promontory, which works for many of the world's largest banks and employs several former senior regulatory officials from the US Federal Reserve and the Office of the Comptroller of the Currency. In the UK, Promontory's non-director chairman is Sir Callum McCarthy, who formerly headed the previous City watchdog, the Financial Services Authority.

In 2012, Standard Chartered paid $667m to DFS, the US Justice Department and other authorities to settle allegations it illegally moved millions of dollars through the US financial system for clients in Iran, Sudan and other countries under sanctions. Last year the London-listed bank, which focuses on emerging markets, was fined another $300m for failing to detect suspicious transactions.

According to Reuters, an anonymous source is quoted as saying "At stake in the investigation is whether Promontory may have amended the report to regulators under pressure from the bank"…. "The concern is they sanitized the report."…"Starting Tuesday, New York plans to depose at least a half dozen employees of Promontory it has subpoenaed".

In recent years, New York regulators have scrutinised the independence of consultants retained by banks to report to regulators. Deloitte LLP agreed in 2013 to pay New York $10 million and stay out of certain business for a year over accusations it watered down a report on Standard Chartered. Last year, PricewaterhouseCoopers paid $25 million and agreed to abstain from certain work for two years over claims it whitewashed a report involving Bank of Tokyo-Mitsubishi UFJ.

3.2 UK FCA Announce New Rules on Remuneration

On 23rd June 2015 the Financial Conduct Authority (FCA) issued their final rules and guidance in relation to remuneration. These latest developments in the regulation of remuneration in the financial services sector form another milestone in the transformation of the regulatory regime which has been on-going since the financial crisis. According to the UK Treasury, Britain now has the toughest rules on bankers' pay of any major financial centre. However, major questions remain unanswered, and bonus disputes appear inevitable once the new rules are applied in practice.

The aim of the FCA's Remuneration Codes is to:

- ensure greater alignment between risk and individual reward
- discourage excessive risk taking and short-termism
- encourage more effective risk management, and
- support positive behaviours and a strong and appropriate conduct culture within firms

The relevant changes apply to banks, building societies and Prudential Regulatory Authority-designated investment firms, including UK branches of non-EEA headquartered firms. The rules must be abided by Material Risks Takers (MRTs) who are within the scope of the remuneration code at these firms, including Senior Managers under the forthcoming Senior Managers Regime from 2016.

The FCA expect that all applicable firms make sure their remuneration policies and practices are consistent and promote sound and effective risk management. This requirements include the following:

- At least 40% of a bonus must be deferred over a period of at least three years. At least 60% must be deferred for the most senior management or when an individual's bonus is a particularly high amount.
- At least 50% of a bonus must be made in shares, share-linked instruments or other equivalent non-cash instruments. These shares or instruments should be subject to an appropriate retention period.
- Ensure guarantees are only given in exceptional circumstances to new hires for the first year of service.
- Ensure senior management adopts and periodically reviews the general principles of the remuneration policy and handles its implementation as well as disclose details of their remuneration policies at least annually.
- Ensure performance is assessed with respect to financial and non-financial factors and is based on the performance of the individual, business unit concerned and the overall results of the firm.
- Ensure that any variable remuneration, including a deferred portion, is paid or vests only if it is sustainable according to the financial situation of the firm as a whole, and justified on the basis of the performance of the firm, the business unit and the individual concerned.

As noted by Martin Wheatley, the CEO of the FCA, these latest rules form 'part of a wider package that is being announced over the summer to embed an accountable culture in the City'. This package forms part of the FCA's policy of credible deterrence through which it will incentivise good behaviour and hold individuals to account, through enforcement action, for misconduct or breach of its rules.

Further information
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4.0 FINANCIAL CRIME UPDATE

4.1 Former "Star Trader" Sentenced to 14 Years Over LIBOR Rigging

Former UBS Group AG and Citigroup Inc. trader Tom Hayes, the first person to stand trial for manipulating Libor, was sentenced to 14 years in prison after being found guilty, in London, of conspiracy to rig the benchmark rate.

The conviction came three years after a then-record fine against Barclays sparked a global outcry over the rigging of benchmarks and billions of dollars in fines.

The jury unanimously found Hayes guilty of eight counts of conspiracy to defraud, after a week of deliberations at the end of a two-month trial.

The Serious Fraud Office argued that Hayes was at the centre of a network of traders at 10 firms that conspired to manipulate the Libor benchmark between 2006 and 2010. Since the scandal was uncovered, more than half a dozen banks have paid billions of pounds in fines and several have fired their chief executives. The sentence is also the latest of a string of harsh punishments handed out to bankers convicted of fraud, which highlight the judiciary's toughening stance on financial crime. Magnus Peterson, the founder of collapsed hedge fund Weavering Capital, was given a 13-year prison sentence earlier this year while UBS rogue trader Kweku Adoboli received seven years in 2012.

Legal experts say Hayes would have been given a considerably shorter sentence had he co-operated fully and pleaded guilty before trial.

Further information
If you would like a more detailed discussion on this update, please contact:
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5.0 ENFORCEMENT ACTION

5.1 State Bank of India Fined in Hong Kong for AML Failures

The Hong Kong Monetary Authority (HKMA) has fined State Bank of India's Hong Kong Branch for violating the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (AMLO) of Hong Kong. HKMA, the monetary and banking regulator of Hong Kong, said the branch of India's largest bank, failed to carry out the customer due diligence measures set out in AMLO rules before establishing business relationships with 28 corporate customers and continuously monitor its business relationships with its customers. The branch also failed to establish and maintain effective procedures for determining whether its customers or beneficial owners of its customers were politically exposed persons and establish effective procedures to ensure compliance with the specified provisions in the AMLO.

The fine marks the first time the HKMA has taken disciplinary action under the AMLO, brought into force in 2012.

Besides paying the fine, the bank must also submit an independent report to the HKMA, outlining the remedial action it will take to tackle these internal control failings, it said.

"It is important to note that neither the HKMA nor the external consultants found any instances of problem accounts or suspicious transactions during the period in question, or the years following," SBI said in a statement.

The HKMA has stepped up efforts to crack down on money laundering in recent years following fears raised by international regulators that the city's controls were not strong enough.

Further information
If you would like a more detailed discussion on these or other enforcement actions, please contact:
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ABOUT CCL

Established in London in 1988, 2006 in Dubai and 2012 in India, CCL provides specialist compliance services to organisations that are either already regulated by the Dubai Financial Services Authority (DFSA), or those that wish to become regulated.

Consultancy & Documentation

Authorisation (Full Project Management)
Pre & Post Authorisation Consultation
Regulatory Analysis, Interpretation and Advice
Compliance Outsourcing
Compliance Documentation
Prevention of Money Laundering and other Financial Crime
Risk Management
Corporate Governance
Capital Adequacy and Prudential Reporting
Forensic Compliance and Enforcement Advice

Training

Governance, Risk & Compliance
Finance Induction
CISI Qualifications

If you wish to discuss how CCL can assist you with any of the issues raised in this Regulatory Update, please contact one of the principals using the details below:

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This Regulatory Update provides information about the consultative documents and publications issued by the DFSA which are still current, proposed changes to the Rules and Guidance set out in the DFSA's Handbook, actual changes to Rules and Guidance that have occurred in the months leading up to the update and other matters of relevance to DFSA-regulated firms. This Regulatory Update is intended to provide general summarised guidance only, and no action should be taken in reliance on it without specific reference to the particular DFSA document referred to.