Thematic Review of the Adoption of the Principles set forth in IOSCO's Report: Recommendations Regarding the Protection of Client Assets

Final Report

THE BOARD

OF THE

INTERNATIONALORGANIZATION OF SECURITIES COMMISSIONS

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1. EXECUTIVE SUMMARY

This report (**Report**) sets out the findings of the Thematic Review (**Review**) by the International Organization of Securities Commissions (**IOSCO**) of the progress jurisdictions have made in adopting legislation, regulation and other policies in relation to IOSCO's *Recommendations Regarding the Protection of Client Assets* (the **2014 Report** or the **Principles**).[1]

The Principles outline:

- The intermediary's[2] responsibility to ensure compliance with rules and regulations governing client assets, including the development of risk management systems and internal controls to monitor compliance;
- The intermediary's responsibility to reconcile the client's accounts and records with those of the third party where the intermediary places client assets with third parties; and
- The regulator's role in supervising the intermediary's compliance with the applicable domestic rules and maintaining a regime that promotes effective safeguarding of client assets.

This Report was prepared by a team (**Review Team**, see **section 3.2**) constituted of IOSCO members of the Assessment Committee, relevant experts from the Committee on the Regulation of Market Intermediaries and the IOSCO General Secretariat. The Review Team drew members from six jurisdictions and was chaired by the US Securities and Exchange Commission (**SEC**).

Background

The Review was a "Level 1" or "Adoption Monitoring" review designed to identify progress of jurisdictions in adopting legislation, regulation and other policies (**Adoption Measures**) in relation to the Principles. This Review does not assess the consistency of Adoption Measures against the Principles.

The Review is based on the implementation progress reported by the jurisdictions (**participating jurisdictions**) as of 30 April 2016 (**Reporting Date**).

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[1] *Recommendations Regarding the Protection of Client Assets*, IOSCO, January 2014, available at: http://www.iosco.org/library/pubdocs/pdf/IOSCOPD436.pdf.

[2] For the purposes of this Review, the Principles are understood to apply to securities firms that hold client assets and are engaged in the business of managing client accounts, which could include, without limitation: executing orders on behalf of others and dealing in or distributing securities (including carrying derivatives positions). In jurisdictions where banks are broadly permitted to engage in such a business, the Principles are understood to apply to banks to the extent they are providing such services. This scope is derived from the definition of 'Investment Firm' used in a survey sent in 2012 to regulators of the IOSCO Committee on the Regulation of Market Intermediaries concerning *Regimes for the Protection, Distribution and/or Transfer of Client Assets*. The results of that survey served as the basis for the Principles.

Thirty-eight IOSCO members from 36 jurisdictions contributed to the Review. A list of participating jurisdictions is set out at **Annex A**.

The Review Team agreed on a standardized approach (**Review Process**, see **section 3.3**) to reporting progress of Adoption Measures under each Principle and reviewed the self-assessments to the Assessment Methodology provided by participating jurisdictions and considered whether and when to challenge those self-assessments. The findings are therefore subject to review (and possible change) by any future assessment that might utilize a different Review Process. Participating jurisdictions were given an opportunity to confirm the self-assessment provided on the progress of Adoption Measures for their jurisdiction and the way it has been reported in this Report.

Key Findings

In general, the Review found that, as on the Reporting Date, the majority of participating jurisdictions has adopted a client asset protection regime described by the Principles. This also includes jurisdictions that, *prior to* the publication of the final Principles, took legislative, regulatory and policy measures that are equivalent in their effect to the Adoption Measures contemplated by the Principles.

Implementation progress varied by jurisdiction. In the EU, most jurisdictions reported having final Adoption Measures across all Principles. Canada and the US have taken Adoption Measures across all Principles, with the exception of Principle 6 being not applicable in those jurisdictions. In some other regions, including Latin America, implementation progress was less advanced.

In addition, progress varied across the Principles. Principles 2, 7 and 8 were the most implemented, with 35 out of 36 jurisdictions having Adoption Measures in place, while Principle 3 was the least implemented, with only 24 out of 36 jurisdictions having Adoption Measures in place.

Participating jurisdictions were found to have either completed Adoption Measures (with a majority completing implementation before the publication of the 2014 Report) or not to have taken Adoption Measures. Only two jurisdictions reported that they were in the process of implementing draft Adoption Measures as of the Reporting Date.[3]

Some jurisdictions were found not to have taken Adoption Measures as described by the Principles due to the manner in which they addressed the holding of client assets by certain categories of market intermediaries within the scope of this report.[4]

[3] Pakistan for Principle 1 and Switzerland for Principles 5 and 6.

[4] Australia, New Zealand and South Africa.

Other jurisdictions that took steps to adopt some aspects of the Principles, but not those key means of implementation (or **MoIs**) the Review Team considered dispositive with regard to the Principles, were also assessed as not having taken Adoption Measures.

The main findings by Principle are:

- On **Intermediary Records (Principle 1)**, 30 out of 36 participating jurisdictions have taken Adoption Measures to segregate each client's assets (securities and monies) from other clients' assets, and from the intermediary's own assets. This includes *generally* requiring intermediaries to maintain information, records and accounting in such a manner as to be able to distinguish accounts of one client's asset from other clients' assets, and from their own assets.

- On **Statement of Accounts (Principle 2)**, all the participating jurisdictions except for one have taken Adoption Measures to implement rules that require intermediaries to provide statements to their clients detailing the assets held for or on behalf of the client. While jurisdictions have taken different approaches on implementation of the Principles, the Review Team found that the frequency of intermediaries providing statements to their clients was, across jurisdictions, generally based on (i) the type of investment services provided by the intermediary, (ii) the riskiness of the client's portfolio, (iii) the clients' specific requests for more frequent statements, and (iv) the client's status or categorization (professional versus retail).

- On **Maintaining Appropriate Arrangements to Safeguard Client's Rights and to Minimize the Risk of Loss and Misuse (Principle 3)**, the Review Team agreed to consider all of the means of implementation (or MoI) along with the text of Principle 3 to assess implementation progress. Based on this approach, the Review Team determined that 24 out of 36 participating jurisdictions have taken Adoption Measures with respect to this Principle.

- On **Understanding of Domestic and Foreign Regimes (Principle 4)**, a majority of participating jurisdictions (30 out of 36) have taken Adoption Measures with respect to Principle 4. Most of these jurisdictions have taken one of the following three approaches: (i) explicitly requiring intermediaries to conduct due diligence on third parties that hold client assets; (ii) designating certain types of regulated entities as approved or acceptable custodians where client assets may be held; or (iii) relying on an intermediary's duty of care or regulatory codes of conduct that apply to an intermediary while dealing with a third-party custodian.

- On **Disclosure regarding Client Asset Protection (Principle 5)**, the Review Team agreed that a participating jurisdiction would be considered to have taken Adoption Measures for this Principle, if it has imposed upon its intermediaries *general disclosure requirements* that could be deemed relevant to the protection of client assets, or, in the alternative, by requiring specific disclosure if a foreign (and not the domestic) client asset regime applies, and that any required disclosure (in either case) must be both

transparent and clear. Based on this approach, the Review Team found that 26 out of 36 participating jurisdictions have taken Adoption Measures with respect to Principle 5.

- On **Waiver or Modification (Principle 6)**, 12 participating jurisdictions reported that this Principle is inapplicable to them, as they do not permit any waiver or modification envisaged under Principle 6. Nineteen out of the remaining 24 participating jurisdictions, which do permit waiver or modification, were found to have taken Adoption Measures with respect to this Principle, including adequate disclosure and retention processes and procedures. One jurisdiction reported to be in the process of implementing draft Adoption Measures. Four participating jurisdictions were assessed having not published draft Adoption Measures.

- On **Compliance with Domestic Requirements (Principle 7)**, the Review Team found that monitoring compliance with a jurisdiction's domestic regime was the key factor in applying Principle 7. The Review Team found all but one participating jurisdiction have taken Adoption Measures to implement this Principle.

- On **Information on Foreign Jurisdictions (Principle 8)**, all but one participating jurisdiction have taken Adoption Measures with respect to Principle 8. The Review Team determined that a jurisdiction would be found to have taken Adoption Measures with respect to this Principle if it has at least entered into cooperation agreements, such as the IOSCO Multilateral Memorandum of Understanding (**MMoU**), or similar arrangements (for either supervisory or enforcement purposes) with other regulators in foreign jurisdictions.

2. BACKGROUND

2.1. IOSCO's Recommendations Regarding the Protection of Client Assets

The 2014 Report contained eight Principles intended to assist regulators in enhancing their supervision of intermediaries holding client assets, by outlining roles of the intermediary and the regulator in protecting client assets. These Principles were developed in response to the greater scrutiny by investors and regulators alike in understanding the potential risks and implications of placing assets with different intermediaries. The Principles are intended to apply to the regulation and oversight of intermediaries and the actual conduct of the intermediaries, including intermediaries' responsibilities and the relationship between an intermediary and its clients.

2.2. Reasons for the Review

In December 2014, based on a submission from the Committee on the Regulation of Market Intermediaries, the Assessment Committee (**AC**) recommended to the IOSCO Board that it perform a Thematic Review of the Principles. The Principles address an important post-Crisis issue of protection of client assets and support the recovery and resolution work of international standards setting bodies. As the Principles target a core investor protection function of all

securities regulation, this Thematic Review should benefit developed as well as growth and emerging market jurisdictions. On 17 December 2015, the IOSCO Board approved the terms of reference for this Review.

3. METHODOLOGY

3.1. Nature of the Review and Objectives

The main objective of the Review was to identify progress of jurisdictions in adopting legislation, regulation and other policies in relation to intermediaries holding client assets addressed by the Principles. The focus of the self-assessments was on each jurisdiction's progress towards establishing the legal capacity to carry out and act in accordance with the Principles. Specifically, the Review Team asked jurisdictions to identify the published and/or in-force source(s) of their legal authority to implement the Principles. The Review also sought to identify differences in approaches and the progress of implementation (or proposed implementation) of the Principles.

While the Review reports on the status of Adoption Measures, it does not assess the consistency of Adoption Measures against the Principles. The Review Team conducted this Level 1, Adoption Monitoring exercise against all the Principles, but differentiated between dispositive and non-dispositive MoIs set out in the 2014 Report (as addressed in **section 3.3**). The differentiation was based on an assessment of the intended effect each MoI contributed to the outcome to be achieved by the Principles. The Assessment Methodology and Questionnaire used by the Review Team and sent to participating jurisdictions for self-assessment purposes is attached as **Annex B (Assessment Methodology and Questionnaire)**.

For the purposes of this Review, the Principles are understood to apply to securities firms that hold client assets and are engaged in the business of managing client accounts, which could include, without limitation: executing orders on behalf of clients/others and dealing in or distributing securities (including carrying derivatives positions). In jurisdictions where banks are permitted to engage in such a business, the Principles are understood to apply to banks to the extent they are providing such services.[5] Based on the glossary provided in the 2014 Report, the Review Team operated on the basis (and clarified where appropriate) that if a respondent used the term "client assets" in its self-assessment, then the relevant legislation, regulation or policies applied, to the extent appropriate, to client positions, client securities and monies held by an intermediary for or on behalf of a client.

3.2. Review Team

The Review was conducted by a team comprised of staff from the following national authorities: George Lavdas and Brandon Hill (Securities and Exchange Commission, US),

[5] This scope is derived from the definition of 'Investment Firm' used in the 2012 survey to regulators of the IOSCO Committee on the Regulation of Market Intermediaries concerning *Regimes for the Protection, Distribution and/or Transfer of Client Assets*. The results of that survey served as the basis for the Principles.

Aliasgar Mithwani and Sanjay Singh Bhati (Securities and Exchange Board of India), Simona Serio (Commissione Nazionale per le Società e la Borsa, Italy), Ivana Sucur, Casper Rutting and Barbara Antonides (Authority for the Financial Markets, Netherlands), Jessica Leung (Ontario Securities Commission), Philippe Marie, Jane Moore and Andrea Ferguson (Financial Conduct Authority, UK) and Raluca Tircoci-Craciun and Anna Zhang (IOSCO General Secretariat) (**Review Team**).

George Lavdas of the US Securities and Exchange Commission chaired the Review Team.

3.3. Review Process

The Review was a desk-based exercise, using responses provided by 38 IOSCO members from 36 jurisdictions to the Assessment Methodology and Questionnaire designed and developed by the Review Team. The Assessment Methodology and Questionnaire was circulated on 29 February 2016, with responses due on 28 March 2016. Late responses were accepted until 30 April 2016. In most cases, the Review Team sought additional information to clarify or verify aspects of responses.

The Assessment Methodology and Questionnaire asked whether the respondent jurisdictions had implemented Adoption Measures in relation to the areas covered by the eight Principles and, if so, for them to indicate the status of such and references to relevant legislation, regulation or policy.

Preparation of this Report

On reporting progress in implementation, the Review Team agreed as follows:

- It would assess implementation progress based on a jurisdiction's response to two types of questions: (i) questions that are dispositive of the rating for the overall Principle[6] and (ii) questions that could elicit useful background, but should not be considered dispositive with respect to this Level 1 review.[7] The Review Team agreed, with the exception of Principles 3 and 5 (see below), that a jurisdiction must satisfy fully the criteria under each dispositive question in the Assessment Methodology and Questionnaire in order to receive an assessment that Adoption Measures were taken under the relevant Principle. Only partially satisfying the relevant criteria for a particular Principle would result in an assessment of "draft Adoption Measures not published".

[6] Questions were deemed dispositive based on their relevance to the key elements and objectives of each Principle in the 2014 Report. The objectives, key elements, and related questions for each Principle are described and discussed in more detail in Section 4.2.

[7] Following an initial review of responses, the Review Team agreed it would could consider responses to non-dispositive questions (questions later "greyed out" in the Assessment Methodology and Questionnaire in **Annex B**), but responses with inadequate regulatory requirements to these questions should not in most cases change a jurisdiction's rating for the overall Principle.

- The Review Team agreed that in order for a respondent to be assessed as having implemented Adoption Measures with respect to a particular Principle, the relevant measures must apply to all market intermediaries as defined by this Review. Adoption Measures, which applied only to some market intermediaries (even where this is determined on a risk-assessment basis) would result in an assessment of "draft Adoption Measures not published".

- Based on the glossary provided in the 2014 Report, the Review Team operated on the basis (and clarified where appropriate) that if a respondent used the term "client assets" the relevant legislation, regulation or policy applied, to the extent appropriate, to client securities and monies held by an intermediary for or on behalf of a client. The Review Team notes, however, that any further "Level 2" review or consistency of implementation review would need to include more detailed questions to ensure that the term "client assets" is understood consistently across jurisdictions and that rules implementing the Principles apply to client positions, client securities and monies, where appropriate.

- Client assets within scope of this report include customer derivatives that are carried by or through market intermediaries, other than derivative market intermediaries (**DMIs**) acting in their capacity as DMIs. The IOSCO OTC Derivatives Task Force has addressed DMI standards independent of the IOSCO Committee on the Regulation of Market Intermediaries, including those relating to the protection of customer assets.[8]

- The Review Team agreed that securities lending is outside the scope of the Review. As a result, arrangements between an intermediary and a client related to securities lending were not considered as an "opt out" or waiver for purposes of evaluating responses to Principle 6.

- The Review Team agreed that respondents should identify the published legislation, regulation or policy underlying the relevant Adoption Measures. Moreover, the legislation, regulation or policy implementing the Principle should be enforceable; mere guidance, unsupported by legislation or regulation, is not sufficient.[9] However, the Review Team did not seek to obtain a full, complete and clear description of each jurisdiction's legal and commercial framework because such analysis was beyond the scope of this Review.

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[8] *See, e.g.*, the OTC Derivatives Task Force Report *International Standards for Derivatives Market Intermediary Regulation*, IOSCO, June 2012, available at: https://www.iosco.org/library/pubdocs/pdf/IOSCOPD381.pdf.

[9] However, specific guidance that draws authority from or implements an enforceable regulation or statute would be sufficient. In other words, if an intermediary does not comply with the requirement, it should be subject to regulatory or enforcement action.

On whether and when to challenge self-assessments, the Review Team agreed that it should limit challenging the ratings in jurisdictions' self-assessments to the following situations:

(i) Where the rating scale had been misapplied (*i.e.*, where jurisdictions claimed Adoption Measures not applicable when that was not the case);

(ii) Where the basis for the claimed status of the Adoption Measures was not clear;

(iii) Where purported Adoption Measures were clearly not related to the Principle(s);

(iv) Where the scope of the applicable Adoption Measures did not cover the full scope of the intermediaries and/or client assets as defined by the Assessment Methodology used in this Review; and

(v) Where the scope of the applicable Adoption Measures did not meet all the dispositive MoIs as determined by the Review Team.

The assessments in the Review are based on information provided by the participating jurisdictions, including copies of published and/or in-force legislation, regulations or policies. The Review Team reviewed the information submitted by jurisdictions for completeness to support the self-assessments. Where necessary, the Review Team contacted participating jurisdictions to clarify and/or verify the statements made by participating jurisdiction in their responses. The Review Team also reviewed the self-assessments to identify where jurisdictions may have interpreted the Principles, MoIs or Questionnaire differently. However, the Review Team did not seek to verify independently all statements provided by participating jurisdictions in their submissions for this Review.

3.4. Participating Jurisdictions

All IOSCO member jurisdictions were invited to participate in the Review. IOSCO Board members as well as Assessment Committee members were expected to participate in this Review.

Thirty-eight IOSCO members from 36 jurisdictions contributed to the Review. A list of participating jurisdictions is set out at **Annex A**.

4. KEY FINDINGS

4.1. Overview of Implementation Progress

This section provides an overview of implementation progress in participating jurisdictions. The implementation status of the eight Principles is set out in the table below. A detailed discussion of implementation on a Principle-by-Principle basis is provided in Section 4.2. Examples of different Adoption Measures taken to implement the Principles are summarized throughout Section 4.2. The inclusion of these examples should not be interpreted as an assessment of the consistency of approaches taken to implement the Principles.

Jurisdictions' implementation progress on each Principle was assessed using the following five-level reporting scale:

Status	Description
Final Adoption Measures taken and in force	This will be reported where Adoption Measures have been taken and are in force. This "green" category also applies to those jurisdictions that, *prior to* the publication of the final Principles, took legislative, regulatory and policy measures that are equivalent in their effect to the Adoption Measures.
Final Adoption Measures published but not yet taken or in force	This will be reported where Adoption Measures have been finalized and approved/adopted but have not been taken or put into force.
Draft Adoption Measures published	This will be reported where proposals about Adoption Measures have been made public, for example, through public consultation or legislative deliberations.
Draft Adoption Measures not published	This is intended to cover those jurisdictions that have intermediaries that hold (or could hold) customer assets, but the respondent jurisdiction has taken no published steps to adopt the Principles.
Not Applicable	This will be reported where Adoption Measures are not needed, *e.g.*, because there are no intermediaries within the jurisdiction that hold (or could hold) custody of customer assets.

In general, the Review found that, as of the Reporting Date, the majority of participating jurisdictions have generally adopted a client asset protection regime described by the Principles.

The Review Team notes that implementation progress varied by jurisdiction. In the EU, most jurisdictions reported having final Adoption Measures across all Principles.[10] Canada and the

[10] This is also due to the transposition in the European Member States of Directive 2004/39/EC (MiFID 1), which provides for a comprehensive client asset protection regime in accordance with the Principles. MiFID 1 will be replaced by a new recast Directive (Directive 2014/65/EU) that will be applicable from January 2018. The recast Directive will continue the MiFID 1 regime, confirming and at the same time further strengthening the client asset protection provisions (for instance, in terms of disclosure requirements).

US have taken Adoption Measures across all Principles, with the exception of Principle 6 being not applicable in those jurisdictions. In some other regions, including Latin America, implementation progress was less advanced. In addition, progress varied across the Principles. Principles 2, 7 and 8 were the most implemented, with 35 out of 36 jurisdictions having Adoption Measures in place, while Principle 3 was the least implemented, with only 24 out of 36 jurisdictions having Adoption Measures in place.

As can be seen in the Table below, jurisdictions were found to have either completed Adoption Measures (with a majority completing implementation before the publication of the 2014 Report) or not to have taken Adoption Measures. Only two jurisdictions reported that they were in the process of implementing draft Adoption Measures as of the Reporting Date.[11]

Some jurisdictions were found not to have taken Adoption Measures as described by the Principles due to the manner in which they addressed the holding of client assets by certain categories of market intermediaries within scope of this report. This group included, for example

- "Providers of financial and intermediary services in general" in South Africa, which are intermediaries that do not operate in the listed environment and are not regulated by the exchange in terms of the SRO model of regulation and the Financial Markets Act, although they are regulated by the Financial Services Board in accordance with the Financial Advisory and Intermediary Services Act.[12]

- A certain category of licensed market intermediaries in Australia that have custody of client assets, but are not subject to Australia's full client asset protection regime.[13]

- Other intermediaries or brokers in New Zealand (who are not discretionary investment management services (**DIMS**), DIMS custodians, a custodian more generally, or NZX participants),[14] but appear to be covered by the Principles. Such market intermediaries

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11 Pakistan has informed the Review Team that new regulations were publicly notified on 24 June 2016 (this was after the Reporting Date of 30 April 2016). They will come into effect upon notification by the Pakistan Federal Government of Part V of the Securities Act, 2015. The regulations are available at https://www.secp.gov.pk/document/securities-brokers-licensing-and-operations-regulations-2016/?wpdmdl=14922. In addition, in November 2015, the Swiss Federal Council adopted the Financial Services Act (**FinSA**) in order to improve client protection. The Council of States (Senate) adopted this act in December 2016; in spring 2017, the second chamber of the Swiss Parliament shall deliberate the dispatch of the act. FinSA applies to financial service providers, advisors and issuers. It therefore appears to apply to market intermediaries covered by this report. FinSA improves client protection primarily by means of new disclosure provisions.

12 Nevertheless, these intermediaries provide financial services and are allowed to receive or hold money and assets for or on behalf of clients, and therefore should be covered by the Principles.

13 These "indirect market participants" are generally themselves clients of full service brokers ("direct market participants"). Yet they also purchase and sell securities on behalf of their clients and have custody of client assets, and hence are covered by the Principles, but are not subject to Australia's Market Integrity Rules (**MIRs**). These indirect market participants account for only around 4% of Australia's market turnover.

14 Providers of DIMS must ensure that client assets are held by a custodian that meets the requirements of the FMC Act. In addition, participants in New Zealand's stock exchange (**NZX**) are also subject to specific client asset protection rules.

must meet all of the obligations of the Financial Adviser Act, but they are not subject to additional requirements that apply to DIMS, DIMS custodians, general custodians or NZX participants.

Other jurisdictions that took steps to adopt some aspects of the Principles, but not those key MoIs the Review Team considered dispositive with regard to the Principles, were also assessed as not having taken Adoption Measures.

Based upon the above scale, the Review Team assessed respondent jurisdictions as follows:

	Principle 1 — Intermediary Records	Principle 2 — Statements of Accounts	Principle 3 — Safeguards	Principle 4 — Domestic and Foreign Regimes	Principle 5 — Disclosure regarding Protection	Principle 6 — Waiver or Modification	Principle 7 — Regulators' Oversight of Compliance	Principle 8 — Information on Foreign Jurisdictions
Argentina								
Armenia								
Australia								
Brazil								
Canada[15]								
Cayman Islands								
China								
Czech Republic								
Denmark								
Dubai International Financial Centre (DIFC)[16]								
Ecuador								
France								
Germany								
Greece								

15 The response for Canada was jointly submitted by the Ontario Securities Commission and Québec Autorité des marchés financiers.

16 The Dubai International Financial Centre (**DIFC**) is a Federal Financial Free Zone administered by the Government of Dubai and established in accordance with United Arab Emirates Federal Law. The financial entities in the DIFC are regulated and supervised by the Dubai Financial Services Authority, which has entered into bilateral and multilateral cooperation agreements.

	Principle 1 — Intermediary Records	Principle 2 — Statements of Accounts	Principle 3 — Safeguards	Principle 4 — Domestic and Foreign Regimes	Principle 5 — Disclosure regarding Protection	Principle 6 — Waiver or Modification	Principle 7 — Regulators' Oversight of Compliance	Principle 8 — Information on Foreign Jurisdictions
Hong Kong								
Hungary								
India								
Italy								
Japan								
Jersey								
Mexico								
Netherlands								
New Zealand								
Pakistan								
Portugal								
Saudi Arabia								
Serbia								
Singapore								
Slovenia								
South Africa								
Spain								
Sweden								
Switzerland								
UAE								
UK								
US								

4.2. Implementation of Progress by Principle

4.2.1. Principle 1 – Intermediary Records

Principle 1. *An intermediary should maintain accurate and up-to-date records and accounts of client assets that readily establish the precise nature, amount, location and ownership status of client assets and the clients for whom the client assets are held. The records should also be maintained in such a way that they may be used as an audit trail.*

The 2014 Report notes that it is an intermediary's responsibility to develop "risk management systems and internal controls to help ensure financial integrity and monitor compliance." As a result, Principle 1 provides that intermediaries should make and maintain accurate and up-to-date records and accounts of client assets. In addition, the 2014 Report stated "where the intermediary places client assets with third parties, the intermediary should reconcile its accounts and records with those of the third party."

Out of 36 participating jurisdictions, the Review Team concluded that 30[17] have taken Adoption Measures with respect to Principle 1. In general, these jurisdictions require intermediaries to segregate each client's assets (securities and monies) from other client assets, and from the intermediary's own assets. Intermediaries in the adopting jurisdictions are obligated to maintain information, carry out record keeping and accounting in such a manner as to be able to distinguish client asset accounts of one client from another, and from their own assets.

The MoIs for this Principle also state that the intermediaries' records should be sufficient to permit external verification of intermediary records. The Review Team agreed that Adoption Measures will be deemed to have been taken if an intermediary's records and accounts are available to be verified, reviewed *or* audited at all times. Of those having Adoption Measures in place, jurisdictions generally followed one of these approaches: (i) requiring records to be maintained in such a manner as to make possible verification (but not necessarily auditing) by persons external to the firm, such as by an independent private firm or regulator, but not *requiring* such verification;[18] (ii) requiring external verification by a local regulator or self-regulatory organization (**SRO**), but not requiring audits;[19] or (iii) requiring audits of each intermediary's records and accounts.[20]

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[17] Armenia, Brazil, Canada, Cayman Islands, China, Czech Republic, Denmark, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, India, Italy, Japan, Jersey, Netherlands, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, South Africa, Spain, Sweden, UAE, UK and US (CFTC and SEC).

[18] Armenia.

[19] Brazil, Saudi Arabia and UAE.

[20] Canada, Cayman Islands, China, Czech Republic, Denmark, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, India, Italy, Japan, Netherlands, Portugal, Serbia, Singapore, Slovenia, South Africa, Spain, Sweden, UK, and US (CFTC and SEC).

The Adoption Measures in participating jurisdictions also generally require intermediaries to reconcile their accounts and records for client assets with the accounts and records of third parties where client assets are held. However, the frequency with which intermediaries must perform such reconciliation varies between jurisdictions. In 14[21] of the participating jurisdictions that have taken Adoption Measures, there is a general requirement that intermediaries reconcile their accounts with the accounts of third parties, but without specifying the frequency of reconciliation. In ten[22] jurisdictions, intermediaries are required to periodically reconcile their accounts with third parties, usually monthly, but as short as a week or as long as six months. In the other six[23] jurisdictions, intermediaries are required to perform daily reconciliations.

As stated above, most jurisdictions that have taken Adoption Measures require intermediaries to maintain information and keep records and accounts that enable them, at any time and without delay, to distinguish assets held for one client from assets held for any other client, and from their own assets. As a result, most intermediaries are required to reconcile their records on an ongoing basis and keep them up-to-date at all times.

Finally, although the implementing methodology may differ between jurisdictions, all of the jurisdictions that have taken Adoption Measures require intermediaries to distinguish accounts held with a third party for the benefit of their clients from those of the intermediary. In general, intermediaries are required to ensure that any client financial instruments deposited with a third party are separately identifiable from financial instruments belonging to the intermediary, by opening an account in the client's name or, if it opens an omnibus account in its own name, indicating that such an omnibus account is for the benefit of its clients. Moreover, the MoIs to this Principle indicate third party custodians holding client accounts (including omnibus accounts in the intermediary's name) should clearly distinguish between the intermediary's own accounts and such client accounts.

One of the six[24] jurisdictions that have not taken Adoption Measures has published draft Adoption Measures. The Securities and Exchange Commission of Pakistan (**SECP**) reported

[21] Armenia, Brazil, Denmark, Ecuador, France, Greece, India, Italy, Japan, Netherlands, Serbia, Spain, Sweden and UAE.

[22] Canada, Cayman Islands, Czech Republic, DIFC, Hungary, Jersey, Portugal, Saudi Arabia, UK and US (CFTC and SEC).

[23] China, Germany, Hong Kong, Singapore, Slovenia and South Africa.

[24] The following jurisdictions were found to have not taken Adoption Measures: Argentina, Australia, Mexico, New Zealand, Pakistan and Switzerland. For example, New Zealand was found as not having taken adoption measures because while they meet all other MoIs, they only partially meet the requirement for reconciliation, i.e., brokers who are not Financial Markets Conduct Act 2013 custodians or NZX participants are not specifically required to reconcile client asset records on any particular frequency. They are only subject to a "general duty of care" in the Financial Adviser Act to reconcile on an "appropriate frequency." In Mexico, while all other MoIs are satisfied, the Mexican regulatory framework does not have an explicit requirement for daily asset reconciliations. However, as market practice, intermediaries perform reconciliations in order to comply with other provisions of the Mexican Securities Law (LMV) and/or the mandatory provisions for broker-dealers which require daily valuation and monthly account statements for clients.

that draft Adoption Measures regarding intermediary obligations to maintain records and accounts have been published in the Pakistan Stock Exchange (**PSX**) rulebook. The draft adoption measures include requirements to segregate clients' assets from one another and the broker's (intermediary) assets. At the Reporting Date, the SECP was consulting on the draft regulations with a view to finalizing them by June 2016.[25] Further analysis after final adoption would be necessary in order to assess whether the draft measures implement this Principle.

4.2.2. Principle 2 – Statement of Accounts

Principle 2. *An intermediary should provide a statement to each client on a regular basis detailing the client assets held for or on behalf of such clients.*

This Principle states that market intermediaries should provide a statement to each client on a regular basis detailing the assets held for or on behalf of such clients. In order to assess adoption of the necessary measures under this Principle, the Review Team relied on participating jurisdictions' descriptions of information and statements that they require an intermediary to provide to its clients, and with what frequency. Although not dispositive of the assessment, the Review Team also asked respondents to describe any requirements they impose upon an intermediary to respond to client requests for information within a specified period.

On the basis of the responses of 36 participating jurisdictions, the Review Team concluded that all of the assessed jurisdictions have taken Adoption Measures, except for Australia.[26] The frequency of the provision of the statements, however, varies between jurisdictions depending on:

(i) The type of the investment service provided by the intermediary;

(ii) The riskiness of the client's portfolio;

(iii) Client's requests for more frequent statements; or

(iv) Client categorization.

In at least 18 jurisdictions,[27] the required frequency varies depending on the type of investment service that is provided by the intermediary to the client. Some of these jurisdictions have less

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[25] Pakistan has informed the Review Team that new regulations were publicly notified on 24 June 2016 (this was after the Reporting Date of 30 April 2016). They will come into effect upon notification by the Pakistan Federal Government of Part V of the Securities Act, 2015. The regulations are available at https://www.secp.gov.pk/document/securities-brokers-licensing-and-operations-regulations-2016/?wpdmdl=14922.

[26] In Australia, the provision of information relating to the client asset protection regime is required in a product disclosure statement, which is delivered to the client at the point of sale and must be updated in the case of changes. No periodic information is required to be provided (although it is a market practice to do so).

[27] Cayman Islands, Czech Republic, Denmark, France, Germany, Hungary, Italy, Netherlands, Portugal, Serbia, Singapore, Slovenia, South Africa, Spain, Sweden, UAE, UK and US (SEC and CFTC).

frequent requirements for intermediaries that solely provide custodial services to the client. At a minimum, intermediaries must provide the client with statements of account annually. In the case of portfolio management, however, intermediaries must provide statements of account more often (for example, quarterly). In some jurisdictions, if the intermediary executes orders on behalf of the client, it must inform the client about the trade each time the settlement is done (transaction confirmation).

Another recurring aspect is the connection between the riskiness of the client's portfolio and the frequency with which statements of account must be provided. In at least 16 jurisdictions,[28] an intermediary may be required to provide a statement of account to the client more frequently based on the composition of the client's portfolio. For example, where there is a leveraged or a margined account, some jurisdictions require the intermediary to provide daily statements of account to the client. India, for instance, has a daily requirement for intermediaries holding collateralized client portfolios.

In at least 20 jurisdictions,[29] clients may request that intermediaries provide more frequent statements of account. For example, the standard requirement in South Africa and Canada is quarterly, but at the client's request, this frequency can be increased to monthly.

Finally, there are sometimes different requirements for retail versus professional clients, depending on the jurisdiction.[30] In 16 jurisdictions,[31] there are less stringent reporting requirements with respect to professional clients. For example, in the DIFC, the frequency of account statements is to be agreed upon in writing between the market intermediary and the professional client, while market intermediaries are required to provide retail clients with monthly statements of account.

4.2.3. Principle 3 – Arrangements to Safeguard Clients' Rights

Principle 3. *An intermediary should maintain appropriate arrangements to safeguard the clients' rights in client assets and minimize the risk of loss and misuse.*

The objective of this Principle is for intermediaries to ensure that client assets are adequately protected when placed at a third party chosen by the intermediary, specifically aiming to

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[28] Cayman Islands, Czech Republic, Denmark, France, Germany, Hong Kong, Hungary, India, Italy, Netherlands, Portugal, Slovenia, South Africa, Spain, Sweden and UK.

[29] Canada, Czech Republic, Denmark, France, Germany, Greece, Hong Kong, Hungary, India, Italy, Japan, Netherlands, New Zealand, Portugal, Slovenia, South Africa, Spain, Sweden, Switzerland and UK.

[30] Other jurisdictions do not distinguish between retail and professional clients. For example, in the US, SRO rules generally require a broker-dealer to send customers, at a minimum, quarterly account statements showing their positions. The account statements must include a description of any positions, money balances and account activity since the firm issued the prior account statement. Industry practice is to send monthly account statements to customers with activity in their accounts during that month.

[31] Czech Republic, Denmark, DIFC, France, Germany, Greece, Hungary, Italy, Japan, Netherlands, Serbia, Slovenia, South Africa, Spain, Sweden and UK.

minimize the risk of loss or misuse. In assessing this Principle and the MoIs, the Review Team applied the following approach.

First, the Review Team concluded that MoI 3, which focused on the intermediary's due diligence with respect to the selection of third parties with whom client assets are placed, could most easily be used to help assess whether a jurisdiction has implemented Adoption Measures. The Review Team therefore agreed that jurisdictions that had such a due diligence requirement would be assessed as taking Adoption Measures with respect to this Principle.

Second, the Review Team also recognized that the "due diligence" MoI 3 was not the only factor that could lead a jurisdiction to implement "appropriate arrangements" to protect client assets, as per the Principle. The Review Team therefore decided to consider all of the MoI and the text of the Principle itself in assessing Adoption Measures and that, where a jurisdiction did not impose upon its intermediaries an affirmative "due diligence" requirement as per MoI 3, the jurisdiction would be assessed as taking Adoption Measures with respect to this Principle, if the other MoIs were satisfied.

The Review Team also agreed that, absent specific obligations contained in legislation, regulation or enforceable guidance, general duties (*e.g.*, duty of care, duty of loyalty or duty to act) were not sufficient to satisfy the Principle. In the Review Team's view, a statute, rule or enforceable guidance that identifies an intermediary's duties and/or obligations is necessary to identify the rules that apply to intermediaries and their activities. Without this guidance, the Review Team cannot assess whether a general duty satisfies this Principle.

Based on the assessments of the 36 respondent jurisdictions, the Review Team assessed 24 as having Adoption Measures in place and 12 as having not adopted measures. Of those jurisdictions viewed as having Adoption Measures in place, 23 jurisdictions require intermediaries to take specific due diligence steps to assess a third party when engaging it to hold assets for the intermediary's clients, and even on an ongoing basis. This includes all EU respondents (by virtue of such a requirement being contained in the MiFID Implementing Directive[32]), and a number of other respondents.[33]

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[32] Article 18 of Commission Directive 2006/73/EC (the **MiFID Implementing Directive**) requires Member States to permit intermediaries to deposit client monies with one of the following: a central bank, a bank authorised either in the EU or outside the EU or a qualifying money market fund. For all but the former, Member States must require intermediaries to "exercise all due skill, care and diligence in the selection, appointment and periodic review" of the chosen institution. As regards financial instruments, Article 17 of the MiFID Implementing Directive requires Member States to permit investment firms to deposit financial instruments held by them on behalf of their clients into an account or accounts opened with a third party provided that the firms exercise all due skill, care and diligence in the selection, appointment and periodic review of the third party and of the arrangements for the holding and safekeeping of those financial instruments. In particular, in both cases, Member States shall require investment firms to take into account the expertise and market reputation of the third party as well as any legal requirements or market practices related to the holding of those client funds and financial instruments that could adversely affect clients' rights.

[33] The EU respondents included the Czech Republic, Denmark, France, Germany, Greece, Hungary, Italy, Netherlands, Portugal, Slovenia, Spain, Sweden and UK. Other countries that fall into this category include

The Review Team also found that, the US SEC has no due diligence requirement under MoI 3 (in contrast to the US CFTC), however, it does have in place Adoption Measures under other MoI. For example, in the US, broker-dealer intermediaries are subject to rules and regulations which safeguard clients' rights in client assets and minimize the risk of loss and misuse, including when client assets are placed with a third party.[34] Finally, US broker-dealer intermediaries are required to segregate client assets from the firm's proprietary business activities and to hold certain client assets free of lien (*e.g.*, segregated cash and fully paid and excess margin securities).[35] If the broker-dealer fails, these client assets should be readily available to be returned to clients.

In general, the 12 jurisdictions found not to have taken Adoption Measures followed one of the following approaches:

Armenia, Australia, Canada, Cayman Islands, DIFC, Japan, Saudi Arabia, Serbia, Singapore, Switzerland and US (CFTC). In addition to due diligence requirements, intermediaries in Canada are also required to use entities that are acceptable by the regulator as custodians for client assets.

[34] In the US, broker-dealers that maintain custody of client assets are required to (i) safeguard client cash and securities; (ii) file a "compliance report" with the SEC to verify they are adhering to broker-dealer capital requirements and protecting client assets they hold (including client assets held at a third party control location); (iii) file a Form Custody that elicits information about the broker-dealer's practices with respect to the custody of client assets; (iv) on a quarterly basis, physically examine and count the securities positions owed to customers and securities on hand (or held at a control location) and reconcile those two numbers; (v) notify the SEC and its designated examining authority (**DEA**) if it fails to maintain certain levels of net capital or under other conditions, designed to provide the SEC with "early warning" that the broker-dealer may experience financial difficulty; (vi) have a supervisory system, including written supervisory procedures, internal operating procedures (including operational and internal controls), and compliance procedures designed to detect and prevent, to the extent practicable, violations of the federal securities law, the rules and regulations thereunder, and the SRO's rules, including safeguarding of client assets; and (vii) appoint a chief compliance officer and certify annually that the broker-dealer has in place policies and procedures to establish, maintain, review, test, and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable rules and regulations, including client asset related matters.

[35] For example, in the US, Exchange Act Rule 15c3-3 requires that every broker-dealer obtain and maintain possession and control of fully paid and excess client securities, and maintain a reserve account that contains (at least) the net dollar amount of cash the broker-dealer owes to its clients. Physical possession or control means the broker-dealer cannot lend or hypothecate these securities and must hold these securities in one of several specified control locations (such as a bank or clearing agency) free of liens, and contracts with each custodian must include certain representations, such as the securities are held free of liens or any other interest that could be exercised by a third party to secure an obligation of the broker-dealer. If a broker-dealer uses a bank (as defined in section 3(a)(6) of the Exchange Act) as a control location, the bank must acknowledge in writing that the securities in its custody and control are not subject to a lien in favor of the bank or any person claiming through the bank. The SEC must approve the holding of client securities at a foreign third-party location. For a foreign control location to be deemed satisfactory, a broker-dealer must represent in an application to the SEC that certain conditions are satisfied, including obtaining a written representation that the securities are not subject to a lien.

In addition, as stated above, a broker-dealer that maintains custody of client assets must maintain a "Special Reserve Bank Account for the Exclusive Benefit of Customers" separate from its other bank accounts. A US broker-dealer must have a written agreement with the bank that the reserve account funds are not to be used directly or indirectly as security for a loan and must maintain a "no-lien letter" from the bank acknowledging this limitation.

a. In Hong Kong, Jersey and the New Zealand, regulators have adopted a partial, limited due diligence approach. For example, Hong Kong has a due diligence requirement for assets placed in a foreign jurisdiction, but this requirement does not apply to assets held in their home jurisdiction. [36] In New Zealand, if a broker outsources client asset handling they are expected to carry out and record a "reasonable level" of due diligence on that third party and the proposed arrangements under the agreement between the broker and the third party. Brokers remain responsible to the client in relation to those services. The guidance provides detailed considerations of what the due diligence should contain. However, these New Zealand due diligence requirements would not generally apply to placing client monies with a bank because it is not considered outsourcing. This approach is similar in Jersey. In sum, since these three jurisdictions have a partial due diligence requirement and do not appear to meet the other MoIs, the Review Team found Adoption Measures have not been taken in these jurisdictions.

b. Seven other jurisdictions[37] have explicit requirements that intermediaries can only use certain types of regulated entities designated by the regulator as approved or acceptable custodians to hold client assets. Intermediaries in these jurisdictions are not required to carry out any additional due diligence on the third party either at the point of selection or on an ongoing basis.

   1. In Argentina, Brazil, Mexico,[38] Pakistan and the UAE, intermediaries are required to hold client securities (not client funds) at a central securities depository (**CSD**). As these jurisdictions did not meet other MoIs under this Principle, the Review Team found Adoption Measures have not been taken in these jurisdictions.

   2. The Review Team found Adoption Measures not taken in China and India[39] because, although their custodians may hold both client assets and monies,

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36 In Hong Kong, under the Securities and Futures (Client Securities) Rules and the Securities and Futures (Client Money) Rules, all client securities received by an intermediary needs to be (i) registered in the name of the client or deposited in an approved institution and (ii) the client money has to be kept in a segregated account for the exclusive benefit of the client with either a person approved by the Hong Kong Securities and Futures Commission (SFC), or an authorized institution regulated by the Hong Kong Monetary Authority. The Code of Conduct for Persons Licensed by or Registered with the SFC requires intermediaries to ensure that client assets are promptly and properly accounted for and adequately safeguarded and that, where a client's assets are received or held overseas, additional risk disclosures should be provided to the client because such assets may not enjoy the same protection as that conferred under Hong Kong legislation.

37 Argentina, Brazil, China, India, Mexico, Pakistan and UAE.

38 For example, in Mexico, intermediaries are required to keep both their own and their clients' securities deposited at a CSD (there is only one CSD in Mexico). Intermediaries are also allowed to place client assets (securities) with a third party as long as they obtain authorisation from the CNBV. In order to obtain authorization, intermediaries must undertake an assessment of the third-party services and be able to monitor and evaluate those services.

39 Under the Securities and Exchange Board of India, Act 1992 and Intermediaries Regulations, all client securities received by an intermediary needs to be (i) registered in the name of the client and deposited in a SEBI registered Depository and; (ii) the client money has to be kept in a segregated account for the exclusive benefit of the clients with a Bank regulated by the Reserve Bank of India. The Code of Conduct for

intermediaries are not required to take any additional steps other than using approved custodians. China, for example, has identified 23 of its banks as having the required qualifications for holding client assets. It has, however, no sufficient requirements in place as to the other MoIs under this Principle.

c. Two additional jurisdictions were found not to have published Adoption Measures. This included South Africa, because it is still in the process of adopting rules related to this Principle for those intermediaries not operating in the listed environment,[40] and Ecuador, because its self-assessment was not responsive to the Principle.

4.2.4. Principle 4 – Understanding of Domestic and Foreign Regimes

Principle 4. *Where an intermediary places or deposits client assets in a foreign jurisdiction, the intermediary should understand and take into account the foreign regime to the extent necessary to achieve compliance with applicable domestic requirements.*

This Principle was intended to encourage regulators to adopt the necessary rules or regulations that would require intermediaries to take the steps necessary to understand the client asset protection regimes and arrangements in every jurisdiction where client assets are kept, to the extent necessary to ensure compliance with domestic requirements. Moreover, if an intermediary places or deposits client assets in a foreign jurisdiction, it should understand and take into account the foreign regime to the extent necessary to achieve compliance with applicable domestic requirements.

The Review Team found that a majority of participating jurisdictions (30 out of 36)[41] took Adoption Measures with respect to this Principle. In general, most jurisdictions have adopted one of the following three approaches:[42]

Intermediaries registered with SEBI requires intermediaries to ensure that client assets are promptly and properly accounted for and adequately safeguarded.

[40] As noted above, in South Africa, there is a certain category of intermediaries that do not operate in the listed environment and are not regulated by the exchange in terms of the SRO model of regulation and the Financial Markets Act. These intermediaries provide financial services and are allowed to receive or hold money and assets for or on behalf of clients, and are therefore covered by the Principles. The Financial Services Board regulates these firms (rather than the Exchange) under the "Financial Advisory and Intermediary Services (**FAIS**) Act." This assessment reflects the status of regulations in this unlisted market rather than the listed environment. The FAIS Act, which applies to intermediaries operating in the unlisted market, does not have the same provisions as the regulations governing intermediaries in the listed markets and the Financial Services Board is still in the process of incorporating the provisions of Principle 3 into the requirements under the FAIS Act. No draft provisions were available and no timeframe for implementation was indicated.

[41] Argentina, Armenia, Canada, Cayman Islands, Czech Republic, Denmark, DIFC, France, Germany, Greece, Hong Kong, Hungary, Italy, Japan, Jersey, Mexico, Netherlands, New Zealand, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, South Africa, Spain, Sweden, Switzerland, UAE, UK and US (CFTC and SEC).

[42] In the UAE, the SCA approves foreign trading where there are contractual provisions in place between the intermediary and client that specify: (i) the process for holding and trading client assets; (ii) a right of recourse for the client; and (iii) a guarantee for the client's assets. In South Africa, neither exchange members nor the CSD hold domestic assets in foreign jurisdictions. With respect to the other intermediaries,

a. Twenty-one jurisdictions[43] explicitly require intermediaries[44] to conduct due diligence in the selection and appointment of third parties that hold client assets in a foreign country. Generally, the responses indicated that intermediaries are required to take into account, among other things, the competence and reputation of the third party, market practices and the applicable regulatory standards on client asset protection, especially when the third party is in a foreign jurisdiction. In addition to due diligence, some jurisdictions have specific requirements on client assets placed in a foreign regime. For instance, all EU jurisdictions allow intermediaries to use a foreign third party to hold client assets *only if* such third party is subject to regulation and supervision over the safekeeping of client assets in its home jurisdiction, unless one of the following conditions is met: (1) the nature of the financial instruments or of the investment services connected with those instruments requires them to be deposited with a third party in that third country, or (2) where the financial instruments are held on behalf of a professional client, that requests in writing that the intermediary deposit them with a third party in that third country.

b. Jurisdictions such as Argentina, Canada, the Cayman Islands, and the US SEC have explicit requirements that intermediaries can use only certain types of regulated entities designated by the regulator as approved or acceptable custodians to hold client assets. Therefore, intermediaries can only use a foreign custodian that meets the standards as set by the regulator. Intermediaries can ensure compliance with domestic requirements when client assets are placed in a foreign jurisdiction by ensuring that the foreign custodian is approved or accepted by the regulator.[45]

c. Three jurisdictions[46] do not have explicit requirements on intermediaries when client assets are placed in a foreign jurisdiction. These jurisdictions rely primarily on a general duty of care and code of conduct requirements on intermediaries when dealing with the use of a third-party custodian. In some cases, they also rely on requirements

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they are subject to the FAIS Act. The FAIS Act specifies the requirements for holding foreign financial products.

[43] Armenia, Czech Republic, Denmark, DIFC, France, Germany, Greece, Hungary, Italy, Jersey, Mexico, Netherlands, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, Spain, Sweden, Switzerland and UK. (The US CFTC requires intermediaries to perform due diligence on depositories that hold customer segregated funds.)

[44] In Mexico, where intermediaries place client assets with the CSD, the duty to review a foreign entity falls on the CSD.

[45] Similarly, in the DIFC and Saudi Arabia, client assets may be placed with a third party in a foreign jurisdiction only if the third-party custodian is subject to regulatory standards that provide equivalent protection compared to a domestic custodian. In the US, the SEC generally does not permit a broker-dealer to hold client cash or domestic securities at a foreign location. A broker-dealer is deemed to have control over foreign securities located in a foreign jurisdiction if the securities are in the custody of a foreign depository, foreign clearing agency or foreign custodian bank, which the SEC upon application from a broker-dealer or upon its own motion designates as a satisfactory control location for securities.

[46] Hong Kong, Japan and New Zealand.

applicable to outsourcing arrangements which require market intermediaries to ensure that client assets held with a third party are adequately safeguarded. To comply with these domestic requirements, intermediaries are expected to obtain an understanding of the regulatory regime of the foreign jurisdiction and assess the adequacy of client asset protection before placing client assets in that jurisdiction.

Three jurisdictions reported "not applicable" under Principle 4 because intermediaries are not allowed to hold client assets abroad (China, India and Pakistan).

Three jurisdictions were assessed as not having taken Adoption Measures with respect to Principle 4, even though intermediaries in these jurisdictions may hold customer assets in foreign jurisdictions (Australia,[47] Brazil and Ecuador). Certain of these jurisdictions, however, have some implied measures that implement this Principle. For example, in Brazil, intermediaries are subject to general conduct rules regarding disclosure of risks and characteristics of products offered to clients, which may require an understanding of the foreign regime.

4.2.5. Principle 5 – Disclosure regarding Client Asset Protection

Principle 5. *An intermediary should ensure that there is clarity and transparency in the disclosure of the relevant client asset protection regime(s) and arrangements and the consequent risks involved.*

This Principle was intended to encourage regulators to adopt the necessary rules/regulations, etc., that would require intermediaries to ensure that there is clarity and transparency in any disclosure of the relevant client asset protection regime(s) and arrangements and the consequent risks involved. As reflected in Principle 6 below, the 2014 Report emphasized the importance of disclosure by intermediaries to clients regarding the scope and breadth of their client asset protection regimes. This emphasis was not only intended to provide greater clarity regarding the status of client assets, but also to permit clients to make informed decisions about whether to consent to any waiver or modification of the client asset protection regime, or whether to opt out. Based upon the context of the Principle in the 2014 Report, and the MoIs thereunder, the Review Team agreed that some kind of disclosure was contemplated by this Principle.

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[47] In Australia, intermediaries have an obligation to hold client property on trust. A trustee has an obligation under general law to exercise the same diligence and prudence as an ordinary prudent person of business would exercise in conducting that business as if it were their own business. A trustee in arranging to hold property in another jurisdiction would be expected to enquire into the way in which the property may be held in that other jurisdiction. The property wherever it is located is required to be held on trust for the client. Although this duty exists under the general law, because there is however no specific obligation contained in statute, rule or enforceable guidance to obtain certain information about how the property is held on trust, the Review Team found that this trust obligation did not satisfy Principle 4.

In developing appropriate benchmarks for applying Adoption Measures, the Review Team focused on the specific elements of the MoIs for guidance.[48]

Based on the MoIs, the Review Team agreed that a respondent jurisdiction would be judged to have taken Adoption Measures with respect to the Principle, if:

- Either:
  - The intermediary is required to disclose to its clients whenever their assets are to be held or placed in a foreign jurisdiction and will be subject to the client asset protection and/or insolvency regimes of that foreign (*i.e.*, not home) jurisdiction;[49] or
  - The intermediary is subject to a disclosure regime, "consistent with the requirements of the home jurisdiction," that client agreements contain "adequate and appropriate information" about the arrangements for client asset protection. According to the above, it would appear that a jurisdiction would meet the Principle if at least general rules covering communications and disclosures to clients were established.[50]
- For each of the above scenarios, requisite disclosure under the client asset protection regime (whether that requirement pertains to the domestic or foreign regime) must be both transparent and clear.

Based on that agreement, the Review Team found that a majority of jurisdictions had adopted an approach that satisfied this Principle through very specific disclosure requirements regarding the applicable client asset protection regime, such as in the EU, or in other

[48] In particular, the MoI 5.2 is very explicit in requiring that:

> Where client assets are to be held or placed in a foreign jurisdiction and will be subject to the client asset protection and/or insolvency regimes of that foreign (*i.e.*, not home) jurisdiction, the intermediary should inform the clients of that fact. The intermediary should, in advance, clearly and in an understandable manner, disclose the risks associated with such client asset custody arrangements and that there may be material differences between the home country and foreign jurisdictions protections and the potential consequences of such differences so the client can make an informed decision concerning its investment.

With regard to other disclosures, the MoI 5.1 states that:

> Consistent with the requirements of its home jurisdiction, an intermediary should ensure its agreements with clients contain adequate and appropriate information about the arrangements for client asset protection and the ways in which the intermediary holds or deposits different types of client assets and the attendant risks. These disclosures should (i) be appropriate in light of the relationship between the client asset and the client's rights in the asset and (ii) take account of the fact that the ownership status of the client assets may affect the degree of protection.

[49] See MoI 5.2. If the domestic regime always applies, then no specific disclosure is required.

[50] See MoI 5.1.

jurisdictions, through more general rules covering communications and disclosures to clients applicable to regulated intermediaries.

Other jurisdictions, such as Australia, were considered not to have satisfied the Principle due to having disclosure requirements at the point of sale of a specific product, similar to "risk factor" disclosure that would be included in a prospectus. Australia's regime does not include disclosure requirements regarding client assets or other specific issues, but rather, requires licensees to disclose (among other things) anything that pertains to significant risks of the product or would otherwise be expected to influence the decision of a reasonable person whether to acquire the product.[51]

Overall, 26[52] out of the 36 participating jurisdictions were assessed as having taken Adoption Measures with respect to this Principle. For example, the EU adopted a comprehensive client asset disclosure requirement under MiFID 1. In the EU, intermediaries must inform clients,[53] among others, (i) that client assets or monies may be held by a third party on behalf of the intermediary in a foreign jurisdiction, (ii) about the consequences of a possible insolvency of the foreign intermediary or custodian and (iii) to what extent the intermediary is liable for the conduct of the foreign intermediary or custodian. In all EU jurisdictions per MiFID 1,[54] intermediaries are also required to inform clients regarding the existence and terms of any security interests or liens on the client's assets. In addition, disclosures to investors in the EU regarding the applicable client asset protection regime must be fair, clear and not misleading.

One jurisdiction (Switzerland) reported to be in the process of implementing draft Adoption Measures.[55]

Outside of the EU, jurisdictions that have taken Adoption Measures with respect to this Principle have used different approaches. For example, the Monetary Authority of Singapore (**MAS**) has adopted detailed rules for appropriate client disclosures, including notifying clients of the terms and conditions in respect of custodial services. If depositing with another custodian, an intermediary in Singapore must disclose the terms and conditions with that custodian before depositing the clients' assets in a custody account. If client assets are deposited with a foreign custodian, the intermediary must obtain client written consent. The

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51 This includes guidance that, where an issuer holds client money, ASIC requires the licensee to clearly and prominently disclose in its product disclosure statement how it deals with client money.

52 Argentina, Armenia, Brazil, Canada, Cayman Islands, Czech Republic, Denmark, DIFC, France, Germany, Greece, Hong Kong, Hungary, India, Italy, Japan, Netherlands, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, Spain, Sweden, UK and US (CFTC and SEC).

53 Article 32 of MiFID Implementing Directive.

54 Article 32, para. 6 of MiFID Implementing Directive.

55 In November 2015, the Federal Council adopted the FinSA, which, among other things, improves client protection by means of new disclosure provisions. The Council of States (Senate) adopted this act in December 2016. In spring 2017, the second chamber of the Swiss Parliament shall deliberate the dispatch of the act.

MAS has prescribed a risk-warning sheet for intermediaries to use, which is designed to be easily understood by investors.

In the US securities sector, broker-dealers are required to provide clients with various disclosures under both SEC and SRO rules related to arrangements for client asset protection. For example, broker-dealers must advise new customers in writing when they open a new account (and annually) about how to obtain information about the Securities Investor Protection Corporation (**SIPC**), including the SIPC brochure.[56] SRO customer account statement rules also require broker-dealers to advise customers that any oral communications should be re-confirmed in writing to further protect the customer's rights, including rights under the Securities Investor Protection Act of 1970 (**SIPA**).[57] Broker-dealers also must make disclosures to clients on specific trading and investment issues that may pose unique risks to client assets, such as risks involved with trading securities in a margin account.[58]

4.2.6. Principle 6 – Waiver, Modification or Opt Out

Principle 6. *Where the regulatory regime permits clients to waive or to modify the degree of protection applicable to client assets or otherwise to opt out of the application of the client asset protection regime, such arrangements should be subject to the following safeguards:*

- *a. The arrangement should only take place with the client's explicit, recorded consent.*
- *b. Before such consent is obtained, the intermediary should ensure that the client has been provided with a clear and understandable disclosure of the implications and risks of giving such consent.*
- *c. If such arrangements are limited to particular categories of clients, clear criteria delineating those clients that fall within such categories should be defined.*

This Principle provides that a regulatory regime should require that intermediaries obtain clear, informed, explicit and documented client consent of any opt out, waiver or modification of the application or the requirements of the client asset protection regime. The Principle, its three subsections and the accompanying MoI describe a number of safeguards where such a waiver, modification or opt out is possible. These safeguards focus on the need for informed client consent based on clear disclosures and the suitability of such safeguards for different classes of clients.

The Review Team notes that the terms "waiver" and "modification" were not defined in Principle 6. In addition, the Review Team learned that different jurisdictions had a spectrum

[56] *See* FINRA Rule 2266.

[57] *See* NASD Rule 2340. In addition, each account statement is required to include a statement that advises the customer to report promptly any inaccuracy or discrepancy in that person's account to the brokerage firm.

[58] *See* FINRA Rule 2264.

of views and perspectives with regard to what those terms meant. For example, some respondents to the questionnaire believed that securities lending and the associated transfer of ownership could be viewed as permitting a waiver, while others did not.[59] In the end, the Review Team decided to treat instances where a jurisdiction may permit a client to enter into a specific transaction, such as stock lending (which may involve transferring the ownership of client assets and waiving rights such as segregation), as not within the scope of this Principle for the purposes of this Review.

Taking the above into consideration, the Review Team determined that 19[60] jurisdictions had taken Adoption Measures with respect to this Principle. Thirteen of these jurisdictions are of the EU. Specifically, the MiFID regime requires intermediaries to categorize their clients as either retail or professional.[61] Retail clients, which enjoy the highest level of client asset protection, can, under certain conditions, choose for an 'opt-up' to be classified as a professional client. As a consequence, with respect to the client asset protection regime, the intermediary's obligation to provide information to professional clients is less frequent. Intermediaries must inform their clients of their classification and obtain confirmation that the customer understands they will be treated as such. Thus, although MiFID implemented a classification system that permits modification of the client asset protection regime in the EU, the classification requires the client's informed consent and there are clear criteria delineating the clients that fall within the different classes.

One jurisdiction (Switzerland) reported to be in the process of implementing draft Adoption Measures.[62]

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[59] In addition, with regard to the EU and some other jurisdictions, the Review Team needed to consider whether where a regulatory regime permits a "retail" client, upon request, to be treated as a "professional" client, this would be deemed to be a modification of the client asset protection regime. This issue arises because under MiFID, for example, professional clients receive account statements less frequently than retail clients. As stated below, the Review Team concluded that an election to be treated as a professional would be viewed as a modification of the client asset protection regime, even if such an election were not viewed as such from, *e.g.*, a MiFID perspective.

[60] Armenia, Czech Republic, Denmark, DIFC, France, Germany, Greece, Hungary, Italy, Japan, Jersey, Netherlands, New Zealand, Portugal, Serbia, Slovenia, Spain, Sweden and UK.

[61] A retail client is any client that is not a professional client; MiFID defines professional clients as including both clients that are considered "per se" to be professional clients and those who may request to be treated as such (see Annex II to MiFID 1). In general, these are clients that possess the experience, knowledge and expertise to make their own investment decisions and properly assess the risks that they incur and include, generally, authorized financial institutions, high net worth companies, regional and local government bodies and certain other institutional investors.

[62] In November 2015, the Federal Council adopted the FinSA, which, together with the Federal Council dispatch, sets out opt-up/waiver provisions between the categories of professional and private clients. The Council of States (Senate) adopted the FinSA in December 2016. In spring 2017, the second chamber of the Swiss Parliament shall deliberate the dispatch of the act. The Federal Council dispatch regularly serve as a source of interpretation of the corresponding acts. In the present case, the dispatch shall serve the Federal Council in the stipulation of its future ordinance. While not legally binding, the Federal Council shall not deviate from its dispatch unless the Federal Assembly would ask it to do so.

Twelve[63] participating jurisdictions reported that they do not permit any waiver or modification envisaged under Principle 6, and therefore that this Principle is not applicable to them.

Four[64] jurisdictions were found to have not taken Adoption Measures for this Principle. These included jurisdictions whose regulations did not prevent such waivers and which therefore did not have accompanying disclosure requirements. On the other hand, some jurisdictions' responses indicated that their regulations did contemplate such waivers, but without requiring disclosures (for example, Cayman Islands).

In addition to the measures discussed above, the MoI also touched on some additional safeguards that intermediaries should implement in connection with a waiver, modification or opt out regarding clarity of documentation, record retention and informed consent. All of the jurisdictions allowing a waiver, modification or opt out had some requirements in place regarding such safeguards. As a result, these jurisdictions were deemed to have taken Adoption Measures.

4.2.7. Principle 7 – Compliance with Domestic Requirements

Principle 7. *Regulators should oversee intermediaries' compliance with the applicable domestic requirements to safeguard client assets.*

Principle 7 deals with regulatory oversight of intermediaries' compliance with the applicable domestic requirements to safeguard client assets. Principle 7 and the accompanying MoIs contemplated that regulators might employ a variety of tools to monitor intermediaries' compliance, including: (i) periodic reporting by intermediaries or SROs; (ii) annual reviews by independent external auditors; (iii) ad-hoc inspections of intermediaries; and (iv) reliance on whistle-blowers to provide information about compliance with domestic requirements.

In addition, the MoIs for Principle 7 envisages that regulators might rely on a risk-based approach that focuses on internal controls to supervise intermediaries' compliance with the applicable domestic requirements. Under such an approach, regulators focus on intermediaries that they believe pose the greatest regulatory concerns. Regulators that adopt such an approach may choose to engage in an in-depth analysis of the value and location of client assets held by intermediaries and their prudential/capital health, liquidity and risk profile. Such an analysis might also include an analysis of the intermediary's general governance, risk management systems and internal control arrangements, regulatory history and complexity of its business, markets in which it operates and customer profiles. In addition to suggesting these potential regulatory approaches, the MoIs of Principle 7 also state that the regulatory regime should

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63 Argentina, Canada, China, Hong Kong, India, Mexico, Pakistan, Saudi Arabia, Singapore, South Africa, UAE and US (SEC and CFTC).

64 Australia, Brazil, Cayman Islands and Ecuador.

clearly describe qualifications for intermediaries to be considered eligible to place or deposit client assets in foreign jurisdictions.

The Review Team agreed that a jurisdiction's approach to monitoring compliance with its domestic client asset protection regime was the most relevant factor in assessing Adoption Measures with respect to Principle 7. In applying this benchmark, the Review Team decided that where information is only collected, but not reviewed, it would not amount to an Adoption Measure with respect to Principle 7. However, the Review Team agreed that a jurisdiction would be found to have taken the necessary Adoption Measures if it performs an assessment of its intermediaries and follows up on it. Regulatory onsite examinations were also considered sufficient monitoring under this Principle.

Although almost all jurisdictions have implemented this Principle, their approaches differ. Based on the Review Team's assessment, 35 of 36 jurisdictions[65] have Adoption Measures in place. One jurisdiction has been assessed as draft Adoption Measures not published.[66] Out of the 35 jurisdictions that have Adoption Measures, 29 jurisdictions[67] employ onsite inspection of intermediaries as a tool for monitoring compliance with their domestic client asset protection regime. Separately, 29 jurisdictions[68] require intermediaries to submit periodic reports; four jurisdictions[69] require SROs to submit periodic reports; and 18 jurisdictions[70] require reporting from external auditors.

Although not dispositive to the assessment against the Principle, the Review Team notes that 27 jurisdictions[71] have adopted a form of risk-based approach to supervising intermediary compliance with their domestic client asset protection regime. Analysis of the responses of the participating jurisdictions reveals that they applied, inter-alia, the following factors for risk-

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[65] Argentina, Armenia, Australia, Brazil, Canada, Cayman Islands, China, Czech Republic, Denmark, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, Italy, India, Japan, Jersey, Mexico, Netherlands, New Zealand, Pakistan, Portugal, Saudi Arabia, Singapore, Slovenia, South Africa, Spain, Sweden, Switzerland, UAE, UK and US (SEC and CFTC).

[66] The exception is Serbia. The Review Team notes that the Securities Commission of the Republic of Serbia adopted a new Supervision Rulebook, which came into force, on 19 August 2016, after the Reporting Date. Under this new Rulebook, Serbian securities authorities will start to apply, as of January 2017, a risk-based approach in its supervision of intermediaries.

[67] Argentina, Armenia, Canada, Cayman Islands, China, Denmark, DIFC, Ecuador, France, Germany, Greece, Hungary, Hong Kong, Italy, India, Jersey, Mexico, Netherlands, New Zealand, Pakistan, Portugal, Saudi Arabia, Singapore, Slovenia, South Africa, Spain, Sweden, UK and US (SEC and CFTC).

[68] Argentina, Armenia, Australia, Brazil, Canada, China, Denmark, DIFC, Ecuador, France, Greece, Hungary, Hong Kong, Italy, India, Japan, Jersey, Netherlands, New Zealand, Pakistan, Portugal, Saudi Arabia, Singapore, Slovenia, South Africa, Spain, UAE, UK and US (SEC and CFTC).

[69] China, India, Pakistan and South Africa.

[70] Australia, Canada, China, DIFC, France, Germany, Italy, Japan, Netherlands, Pakistan, Portugal, Saudi Arabia, Singapore, Slovenia, South Africa, Spain, Switzerland and US (SEC and CFTC).

[71] Australia, Brazil, Canada, Cayman Islands, Czech Republic, DIFC, France, Germany, Greece, Hungary, Hong Kong, Italy, India, Japan, Jersey, Mexico, Netherlands, New Zealand, Portugal, Saudi Arabia, Singapore, South Africa, Sweden, Switzerland, UAE, UK and US (SEC and CFTC).

based supervision: (i) size, (ii) volume of deposits, (iii) intermediary's market share, (iv) client complaints, (v) an intermediary's previous compliance with the respective requirements, and (vi) findings from other sources such as thematic reviews, publicly available information and information from other competent authorities.

Another non-dispositive question posed in the Assessment Methodology and Questionnaire underneath this Principle asked participating jurisdictions about how they might regulate market intermediary eligibility to deposit client assets in foreign jurisdictions. The Review Team considered these responses in completing its assessment although, as stated above, the Review Team viewed a jurisdiction's approach to monitoring compliance with its domestic client asset protection regime as the most relevant factor in assessing Adoption Measures with respect to Principle 7.

The Review Team found that 32 participating jurisdictions[72] allow intermediaries to deposit client assets in foreign jurisdictions, at least to some degree (*i.e.*, foreign securities are permitted to be held in foreign jurisdictions). Three jurisdictions[73] do not allow intermediaries to deposit client assets in foreign jurisdictions and two other jurisdictions[74] did not submit a response to this question.

Out of the 32 jurisdictions that allow such deposits in foreign jurisdictions, 14 jurisdictions[75] have no additional eligibility requirements to make such deposits beyond the general eligibility requirements applicable to all intermediaries (see discussion under Principle 3 regarding the requirements placed on intermediaries prior to making deposits in foreign jurisdictions).

4.2.8. Principle 8 – Information on Foreign Jurisdictions

Principle 8. *Where an intermediary places or deposits client assets in a foreign jurisdiction, the regulator should, to the extent necessary to perform its supervisory responsibilities concerning applicable domestic requirements, consider information sources that may be available to it, including information provided to it by the intermediaries it regulates and/or assistance from local regulators in the foreign jurisdiction.*

Principle 8 addresses the ability of regulators to perform their supervisory responsibilities regarding intermediaries' compliance with the applicable domestic requirements on client asset protection whenever they place or deposit client assets in a foreign jurisdiction. In particular, this Principle recommends that a domestic regulator, to the extent necessary to perform its supervisory responsibilities concerning applicable domestic requirements, considers

[72] Armenia, Australia, Brazil, Canada, Cayman Islands, Czech Republic, DIFC, Ecuador, France, Germany, Greece, Hungary, Italy, Japan, Jersey, Hong Kong, Mexico, Netherlands, Portugal, Portugal, New Zealand, Saudi Arabia, Serbia, Singapore, Slovenia, South Africa, Spain, Sweden, Switzerland, UAE, UK and US (SEC and CFTC).

[73] China, India and Pakistan.

[74] Argentina and Denmark.

[75] Brazil, DIFC, Ecuador, Germany, Hong Kong, Japan, Jersey, Mexico, Netherlands, New Zealand, Portugal, Serbia, South Africa and Saudi Arabia.

information sources that may be available to it, including information provided to it by the intermediaries it regulates and/or assistance from regulators in foreign jurisdictions.

The Review Team notes that the language used in this Principle is quite general and it would benefit from additional interpretive guidance. Therefore, after considering the language of the Principle and the MoIs thereunder, the Review Team agreed that the threshold for implementation under this Principle should be relatively low. Indeed, Principle 8 states that a regulator should "*consider* information sources that may be *available* to it" (emphasis added) in performing its supervisory responsibilities regarding client assets placed or deposited in a foreign jurisdiction. The wording of the Principle (that a regulator should *consider* the information *available* to it) was interpreted by the Review Team to mean the Principle did not suggest the regulator should enter into or seek to enter into multilateral, bilateral or ad hoc arrangements or agreements with foreign regulators related to client asset protection in order to have practices consistent with this Principle.

As such, the Review Team determined that if a jurisdiction has entered into cooperation agreements, such as the IOSCO Multilateral Memorandum of Understanding (**MMoU**), or similar arrangements (for either supervisory or enforcement purposes) with other regulators in foreign jurisdictions that would be sufficient basis to assess that the jurisdiction had taken Adoption Measures to *consider* information sources *available* to it.[76]

Thirty-three[77] jurisdictions reported having taken Adoption Measures with respect to the Principle through arrangements they have to share information with foreign regulators concerning the domestic client asset protection regime. In particular, these jurisdictions are all signatories to the IOSCO MMoU. The IOSCO MMoU establishes a general framework on cooperation in enforcement related matters, which could include the sharing of relevant information in relation to client assets placed in a foreign jurisdiction. In addition, 24 jurisdictions[78] also reported having signed several bilateral cooperation arrangements, establishing a general framework for the sharing of information for supervisory purposes, including in relation to the client asset protection regime.[79] Only one jurisdiction[80] reported

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76 The Review Team notes, however, that although most of the respondent jurisdictions were assessed to have taken Adoption Measures under this Principle, it does not mean that these jurisdictions are actively cooperating with foreign regulators to supervise compliance with their domestic client asset protection regime.

77 Argentina, Australia, Brazil, Canada, Cayman Islands, China, Czech Republic, Denmark, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, India, Italy, Japan, Jersey, Mexico, Netherlands, New Zealand, Pakistan, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, Spain, Sweden, Switzerland, UAE, US (SEC and CFTC).

78 Argentina, Canada, Cayman Islands, China, DIFC, Germany, France, Hong Kong, Hungary, India, Italy, Japan, Mexico, Netherlands, New Zealand, Portugal, Singapore, Slovenia, Spain, Sweden, Switzerland, UAE, UK and US (SEC and CFTC).

79 Some regulators also reported that the exchange of information with foreign counterparties might be subject to confidential treatment: Canada, Greece, Italy, Mexico, Spain and US SEC.

80 Armenia reported that it is taking steps to become a signatory to the IOSCO MMoU.

neither having nor publicly proposing the introduction of arrangements and processes in this regard.

Furthermore, the overwhelming majority of jurisdictions[81] reported having requirements in force to ensure that the regulator has access to all the available information needed to perform its supervisory responsibilities. In addition, a majority[82] of participating jurisdictions reported having reporting requirements and other specific obligations for intermediaries concerning the operation of the client asset regime in foreign jurisdictions.

For example, under MiFID, EU jurisdictions require investment firms to ensure that their external auditors report at least annually to the competent authority on the adequacy of the firm's arrangements to protect client assets. In addition, several[83] EU jurisdictions also require supervised entities to provide other forms of periodic reporting on how they comply with their obligations concerning client asset protection, while other EU regulators primarily rely on the supervisory outcomes of external audit firms' examinations[84] to verify compliance with client asset protection rules.[85]

In order to check intermediaries' compliance with the applicable domestic regime on client asset protection, in addition to information sharing arrangements with foreign authorities, some regulators use public sources of information and/or periodic reporting by intermediaries (such as data on the use of foreign custodians),[86] along with dedicated checks on the information transmitted by the intermediaries concerning the assets placed in a foreign jurisdiction, such as

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81 Armenia, Brazil, Canada, Cayman, Islands, Czech Republic, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, Italy, Japan, Jersey, Netherlands, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, Spain, Sweden, Switzerland, UAE, UK and US (SEC and CFTC).

82 Canada, Cayman Islands, Czech Republic, Denmark, DIFC, Ecuador, France, Germany, Greece, Hong Kong, Hungary, Italy, Japan, Portugal, Saudi Arabia, Serbia, Singapore, Slovenia, Spain, Sweden, UAE, UK and US (SEC and CFTC).

83 Czech Republic, Hungary, Italy, Portugal, Slovenia and UK.

84 France, Germany and Greece.

85 Other sources of information used by EU regulators include consumer complaints, contracts/agreements signed between the investment services provider and foreign jurisdiction, compliance function reports, statistical data on holdings of each client, balance sheet information, data collected from CSD and custodians/sub-custodians, information received from other supervisory authorities, and information collected through the regulator's investigations, including through onsite inspections and analysis of the foreign jurisdiction regulatory framework.

86 *See, e.g.,* Canada. See also responses from some South American and Caribbean countries, which reported that their primary source of information regarding assets held abroad comes from the periodic reporting submitted by intermediaries. For example, in Ecuador, intermediaries are under an obligation to submit to the regulator information on the transactions in foreign jurisdictions the same day that they were carried out, without however specifying the specific details requested in this regard. By contrast, in the Cayman Islands, before an inspection, the regulator requests the intermediary to respond to a self-assessment questionnaire, which would also cover the custodian used, as well as the procedures and processes in place to comply with the domestic client asset protection regime and related evidence.

the records on the due diligence performed by the intermediary, auditor reports, and other documentation transmitted in accordance with periodic reporting requirements.[87]

5. CONCLUSIONS

The objective of this Review was to assess the progress jurisdictions have made in adopting legislation, regulation and other policies in relation to market intermediaries holding client assets, as addressed in the 2014 Report. Jurisdictions were asked to identify the published requirements (legislative, regulatory and policy measures) that implement (or are proposed to implement) the Principles. Mere guidance was deemed insufficient. Where necessary, the Review Team contacted respondents to clarify and/or verify the statements made by participating jurisdiction in their responses to the self-assessment.

In assessing whether a jurisdiction met the objectives of a Principle, the Review Team relied on the Principles and guidance provided in the 2014 Report, including in the MoIs, and explanatory notes to the Principle or elsewhere in the report. The Review Team used these components to inform its interpretation about the core elements of each of the Principles and as a framework for its assessment. Thus, the clarity of each Principle, the MoIs and scope of the 2014 Report were collectively important to the Review Team's assessment of whether a jurisdiction has adopted (or is adopting) measures under each Principle. The Review Team was also able to provide, where relevant, a discussion of the different Adoption Measures taken by the participating jurisdictions implementing, or proposing to implement, the Principles.

Overall, implementation progress varied by jurisdiction and by Principle. In the EU, most jurisdictions reported having final Adoption Measures across all Principles. Canada and the US have taken Adoption Measures across all Principles, with the exception of Principle 6 being not applicable in those jurisdictions. In some other regions, implementation progress was less advanced. In addition, as discussed above, progress varied across the Principles, from Principles 2, 7 and 8 being the most implemented, with 35 out of 36 jurisdictions having Adoption Measures in place, to Principle 3 being the least implemented, with only 24 out of 36 jurisdictions having Adoption Measures in place. Only two jurisdictions reported to be in the process of implementing draft Adoption Measures.

In summary, the Review Team is confident that the Review provides a useful depiction of the current implementation status of the Principles in the participating jurisdictions and that the majority of participating jurisdictions have generally adopted a client asset protection regime described by the Principles.

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[87] DIFC, Saudi Arabia and UAE.

ANNEX A – LIST OF PARTICIPATING JURISDICTIONS

1. Argentina (Comisión Nacional de Valores)
2. Armenia (Central Bank of Armenia)
3. Australia (Australian Securities and Investments Commission)
4. Brazil (Comissão de Valores Mobiliários)
5. Canada (Ontario Securities Commission and Québec Autorité des marchés financiers)
6. Cayman Islands (Cayman Islands Monetary Authority)
7. China (China Securities Regulatory Commission)
8. Czech Republic (Czech National Bank)
9. Denmark (Financial Supervisory Authority)
10. Dubai International Financial Centre (DIFC)
11. Ecuador (Superintendencia de Compañias, Valores y Seguros)
12. France (Autorité des marchés financiers)
13. Germany (Bundesanstalt für Finanzdienstleistungsaufsicht)
14. Greece (Hellenic Capital Market Commission)
15. Hong Kong (Securities and Futures Commission)
16. Hungary (Magyar Nemzeti Bank – Central Bank of Hungary)
17. India (Securities and Exchange Board of India)
18. Italy (Commissione Nazionale per le Societá e la Borsa)
19. Japan (Financial Services Agency)
20. Jersey (Jersey Financial Services Commission)
21. Mexico (Comisión Nacional Bancaria y de Valores)
22. The Netherlands (Authority for the Financial Markets)
23. New Zealand (Financial Markets Authority)
24. Pakistan (Securities and Exchange Commission)
25. Portugal (Comissão do Mercado de Valores Mobiliários)
26. Saudi Arabia (Capital Markets Authority)
27. Serbia (Securities Commission)
28. Singapore (Monetary Authority of Singapore)
29. Slovenia (Securities Market Agency)
30. South Africa (Financial Services Board)
31. Spain (Comisión Nacional del Mercado de Valores)
32. Sweden (Finansinspektionen)
33. Switzerland (Swiss Financial Market Supervisory Authority)
34. United Arab Emirates (Securities and Commodities Agency)
35. United Kingdom (Financial Conduct Authority)
36. United States of America (Commodity Futures Trading Commission and Securities and Exchange Commission).

ANNEX B – ASSESSMENT METHODOLOGY AND QUESTIONNAIRE

Available at: https://www.iosco.org/library/pubdocs/pdf/IOSCOPD577-Annex-B.pdf