Deloitte Regulatory and Financial Crime Conference

8 October 2019

Risks, threats and potential opportunities for the financial services industry and how the industry is dealing with a new set of normals in an increasingly disrupted world

Bryan Stirewalt

Chief Executive, DFSA

Opening Remarks:

Good Morning Ladies and Gentlemen,

It is a pleasure to be here with you all this morning. I would like to begin by extending my sincere thanks to Deloitte for inviting me to participate in today's conference. It is an honour to speak at the Regulatory and Financial Crime Conference this year, and I am looking forward to hearing the views shared in the panel discussions over the course of the day.

Before I begin my specific remarks, I am sure most of you are already aware that the DIFC recently placed eighth on the Global Financial Centres Index. The DIFC's inclusion in the top ten of this important index reflects the dedication and vision of His Highness Sheikh Mohammed bin Rashid Al Maktoum, Vice President and Prime Minister of the UAE and Ruler of Dubai, to develop and grow the DIFC into world-class financial hub. We recently reached an important milestone in the 15-year history of the DIFC with the 500th active financial institution in the Centre. We look forward to continued growth of the Centre in its support of the UAE's economy, and with economies across the region.

As the independent financial services regulator of the DIFC, the DFSA has nearly 170 employees, representing more than 20 different nationalities. I am proud to say that the largest single nationality is the growing group of talented UAE Nationals. I am particularly proud of our growing UAE National population, which is a key priority for the DFSA. The DFSA constantly seeks to empower and support young talent, as they are the resource for sustainable development, growth and prosperity of the UAE. Our Tomorrow's Regulatory Leaders (TRL) programme has yielded positive results for the DFSA and for the UAE, with TRL graduates taking up leadership positions. UAE Nationals now represent 35% of our regulatory workforce.

While these accomplishments are certainly positive, we must be cognisant that we are living in an ever-more uncertain world with new risks and threats, but also with many new opportunities. Several geopolitical challenges have damaged considerable progress in globalisation and trade, yet we are meeting these challenges with determination.

As many of you know, I have the privilege and honour to be the Co-Chair of the Basel Consultative Group, which provides a forum for deepening the Basel Committee's engagement with supervisors around the world on banking supervisory issues. In our meeting last week, members of the Consultative Group noted the growing list of non-traditional risks that now have a distinct impact of banking supervision activity in every country.

Over the course of our meeting last week, we spent a great deal of time discussing climate change risks. On this note, I am proud to say that the DFSA has recently joined the Network for Greening of the Financial System, which was established in December 2017 by a group of central banks and supervisors. The Network's purpose is to help strengthening the global response required to meet the goals of the Paris agreement and to enhance the role of the financial system to manage risks and to mobilize capital for green and low-carbon investments in the broader context of environmentally sustainable development. While one can argue about what to do with climate change risks, I do not believe that anyone can effectively argue that climate change is not happening. This risk must be addressed, and sooner rather than later. The Network is providing a good start toward a long-term and difficult problem.

At the same meeting last week in Basel, we also spent a great deal of time discussing other non-traditional risk areas, including financial crime risks and operational risks, specifically risks emanating from new technology, including cyber risks. We restructured our Supervision Department at the DFSA in 2018 to highlight operational and technology risks in the financial sector. This discussion of new and challenging risks brings us to today's agenda.

Financial Crime

Let us start with financial crime risks. This remains a top regulatory priority for the DFSA. Our Board of Directors has emphasised the need to deal with this risk in a proactive manner since the inception of the Centre 15 years ago, and the need for this emphasis has not subsided. The Board's Risk Tolerance feeds into the DFSA's regulatory priorities and this directs the prioritisation of our resources. This also influences our business activities such as licensing, supervision and enforcement, and our policy and implementation of international standards set by the FATF.

Any mature financial center has incidences of misconduct. However, as a regulatory body, we are constantly evaluating our rules, systems, and processes to ensure what we do remains relevant to the firms and institutions that we regulate. We have shown that we take enforcement of our rules seriously. Our mandate includes the following: fostering fairness, transparency and efficiency in the financial services industry; maintaining financial stability; restraining conduct that may cause harm to the reputation of the DIFC; and protecting direct and indirect users of financial services that delivered in or from the DIFC.

In the past year, we have taken steps to strengthen our enforcement activity, which includes a revamp of our processes and procedures and enlisting the use of enhanced forensic technology in investigations. The first half of 2019 has seen us take nine enforcement actions, with more expected to be finalised in the final quarter of this year. We have placed an emphasis on imposing credible deterrents – as seen in some of our more recent enforcement actions – to discourage others considering engaging in misleading conduct and to prevent future breaches of our rules. We will focus, at all times, our enforcement activity on individuals for responsibilities rather than inanimate shareholders.

As the anti-money laundering (AML) supervisory authority responsible for financial institutions and Designated Non-Financial Businesses and Professions (DNFBPs) operating in and from the DIFC, the DFSA and our other UAE regulatory peers and government authorities share a common goal in fighting financial crime. Overall, the UAE, including the DFSA, focuses its effort on achieving compliance with the international standards for combating financial crime and terrorist finance and promoting sanctions compliance issued by the Financial Action Task Force (FATF).

The DFSA recently participated in an onsite evaluation of the UAE by the FATF, which required significant time, effort and resources from across the organisation over the past two years. I note the next panel discussion today is on Financial Action Task Force (FATF) considerations for the UAE, which also includes some speakers who were heavily involved in this process through preparations and responses to the onsite visit by the FATF Assessors.

The DFSA carries out is efforts to combat financial crime under the AML/CTF framework of the UAE. Some of the key initiatives and positive developments at the UAE and DIFC level relating to ML/TF risks include:

- a new UAE Federal AML Law and By-Laws that were issued in November 2018 and January 2019 respectively, and a new Federal cabinet resolution on the UAE's AML/CTF and Sanctions Compliance framework;
- an updated suspicious activity reporting framework under the UAE's Financial Intelligence Unit (FIU) though the adoption of the "GO AML" application that will significantly assist the UAE with identifying trends, issues and typologies;

- a series of updates to the DFSA's AML Module in the past two years to further align its regime with the FATF Recommendations and the new Federal AML Law; and,
- a new set of beneficial ownership regulations issued in 2018 by the DIFC's Registrar of Companies.

Similar to many of our financial institutions, the DFSA is also making better use of technology to assist both its regulated entities and the DFSA is obtaining more timely and relevant information to assist with our risk-based approach to regulation. For example, the DFSA digitalised its annual AML Return in 2017, which has greatly improved our data analysis capability in this area.

The DFSA remains committed to the fight against illicit finance and we are proud of our accomplishments along the way. However, we can only do this in collaboration with our regulated community and other key stakeholders. These include government authorities, domestic and foreign regulators and law enforcement agencies, and corporate registrars including the DIFC Registrar of Companies. Combatting financial crime is most effective with public / private partnerships working together with a common goal. Most of all, we acknowledge that we must continually adapt and evolve as financial criminals are adapting and evolving too.

The Future of Regulation and Finance – Transformation and Disruption in Financial Services

Now, let us turn to another bit of adaptation, technology. Technology has become a core component and catalyst for change in the global financial services industry. The application of technology to financial services is nothing new – it has been the norm since the 1970s. The difference – at this time – is simply the speed of change.

I continuously reflect on a remark by Bill Gates, many years ago, that banking is a necessary part of every economy, but banks do not necessarily need to be part of it. This quote brought hearty laughter twenty years ago; it brought nervous laughter five years ago; and it brings general nods of agreement today.

We are seeing that many parts of traditional financial services business models can be adapted for the better using the greater computing capacity and newer technologies now available. These new technologies have the potential to enhance customer experiences in the financial sector; improve the efficiency of markets, including trade finance; improve financial inclusion and reduce remittance costs for many economically disadvantaged people; and, enhance security and compliance measures.

In the post-crisis era, those seeking to disrupt the financial sector have spurred much of the transformation we have witnessed. While some disruptive challengers are competing with established financial services firms to take their market share, others are just looking to engage and collaborate. The relationship between the disruptors and the traditional players can be complex. We are seeing large, already established financial institutions looking to “up their game” through Fintech partnerships for better customer experiences. We are also in the nascent stages of seeing “Big Tech” companies such as Apple, Google, Alibaba and Tencent taking a more active look at financial services, in no small part because of consumer trust in their brands and the number of customers in their private ecosystems.

Improving customer experiences is at the heart of change – and this means a lot more than just customer service these days. While what **customer service** encompasses is usually reactive, **customer experience** refers to a customer’s overall journey from start to finish, including every touchpoint and interaction along the way. This is evolving rapidly and may include anything from being able to access an account from multiple channels, to having a question answered immediately by a chatbot or robo-advisor, to receiving automated real-time notifications.

The DIFC Embraces Innovation

In the DIFC, we have embraced the National Innovation Strategy and there is a strong focus on supporting innovation through the **DIFC FinTech Hive**. The Fintech Hive was established in 2017 to support the innovative ecosystem in the DIFC. The Hive programme gives all types of technology firms access to accelerator programmes, mentorship from leading global and local financial institutions, a dedicated cost-effective space to work, a community of like-minded individuals, and access to products and services in front of the region's largest financial community. There are currently more than 80 firms from more than 30 countries registered in DIFC Fintech Hive, with over 40 start-ups having been through their accelerator programmes. The fourth accelerator programme has just commenced with 31 innovative firms from all over the globe participating.

To complement the DIFC Fintech Hive, the **DFSA established the Innovation Testing Licence (ITL)** – a licensed regulatory sandbox. The ITL allows firms to test and develop innovative business models, products and services in or from the DIFC without being subject to the full regulatory requirements that normally apply to Authorised Firms.

Through the ITL:

- We are working with firms that are tokenising traditional securities offerings, digitising sukuk offerings with smart contracts, tokenising crowdfunding campaigns, and offering Artificial Intelligence and Machine Learning-based lender aggregation.

- We are seeing continued interest, in general, in the payment sector and new interest in the field of Stablecoins. We are seeing less interest to introduce new crypto currencies, but continued interest in offering crypto currency trading platforms.

- In terms of RegTech side, we are seeing:

  - increasing interest in the use of distributed ledger-based KYC and digital on boarding, which we support in terms of making customer due diligence and know your customer principles more efficient;

  - increasing interest in the use of biometric identification solutions;

  - increasing numbers of Artificial Intelligence-based financial crime (transaction monitoring) solutions. The goal of these solutions is to reduce the number of false positives and hence provide CDD functions more time to address true positives, and,

  - increasing adoption of blockchain technologies.

Level 13, The Gate, PO Box 75850, Dubai, UAE
Telephone: +971 (0)4 362 1500
Fax: +971 (0)4 362 0801

Other regulators in the region are also supporting digital transformation in financial services, for example in Saudi Arabia earlier this year, the Saudi Arabian Monetary Authority launched a regulatory sandbox to understand and assess the impact of new technologies in the market, allowing local and international firms to enter the Kingdom to do so. Bahrain has also been extremely active with the Central Bank of Bahrain having set up a regulatory sandbox in June 2017 to allow firms to test innovative products and services.

This also highlights the importance of global cooperation in this rapidly changing field. The DFSA joined the **Global Financial Innovation Network (GFIN)** as a way to collaborate with cutting-edge regulatory agencies around the world to promote consistent regulatory engagement, and increase the speed of cross-border adoption of emerging technologies. In order to allow innovative firms to scale new technologies across multiple jurisdictions, GFIN announced a cross-border testing pilot in early 2019. Demand for this cross-border testing was high and we are working with firms in the pilot programme to improve the inefficiencies of working between multiple markets. Governments cannot simply say, “not here”, because “here” is also hard to define with web based products and services.

The DFSA Does Its Part to Promote Innovation

The DFSA is committed to helping the **UAE's National Innovation Strategy** set out by His Highness Sheikh Mohammed Bin Rashid Al Maktoum's aim to create an innovation-friendly ecosystem. This ecosystem is critical to support the digital transformation in the UAE, with one of its key work streams to establish a stimulating environment for innovation in the form of supportive institutions and laws.

Innovation is a key strategic theme and focal point for the DFSA. Facilitating the development of technology in the DIFC and the region by taking steps to understand the risks and opportunities posed in the delivery of financial services. Many say that regulators are resistant to change, however I do not think that is true. Regulators have the difficult job of taking an objective approach to technology, and this includes:

- protecting direct and indirect users of financial services;
- balancing fairness, transparency and efficiency in the market;
- maintaining financial stability; and,
- protecting the reputation of the financial services industry.

Managing all of these objectives takes some juggling, but it would be wrong to say we are resistant to change or unwilling to listen. A regulator's mandate does not carve out innovation from the rules and regulations that govern financial services. We must ensure that all innovators have carefully considered protecting consumers and fighting financial crime. Without meeting both of these considerations, a financial services business cannot begin.

A Data Driven World

Data is the new currency in today's digital world. With the advent of technology, the volume of data generated by financial institutions has grown in leaps and bounds. In this climate, banks and other financial institutions are adapting, sometimes by force, to data-driven organisations. Big data is making inroads into providing critical information for marketing and sales, operations, business performance, and risk management. However, being a data-driven organisation brings forth the challenges of managing big data and its compound characteristics.

Financial services institutions have found ways to **unlock the value of a vast amount of the data** they hold and use it to enable greater insight into their customers. This allows them to anticipate their customer's needs, increase their involvement in their customer's journey, and if I am honest, use that data to develop more products, cross-sell products and services and to obtain enhanced insight of customer purchasing behaviours.

Level 13, The Gate, PO Box 75850, Dubai, UAE
Telephone: +971 (0)4 362 1500
Fax: +971 (0)4 362 0801

In this data-driven world, data analytics is critical for a better understanding of consumer behaviour, meeting regulatory requirements, and generate new sources of revenue. Across industries, business leaders are working on embedding analytics into decision-making and operational workflows. Driving these analytics are visualisation engines that empower users to derive insights toward better risk management, increased profitability, and enhanced growth performance.

In order to counterbalance this increased use of data, there is now an **increasing amount of regulation in this area**. Firms now must think about data privacy and data protection in a new ways, which has presented financial services institutions – and regulators – with an increasing challenge in regards to how to meet these additional requirements.

New systems and controls are needed to ensure appropriate protection of individuals' personal data, as well as new reporting requirements to ensure compliance. There is also the potential for large fines and penalties if these regulations are breached. The localisation of data is also an issue, posing challenges especially to globally active firms. While it might be easy to think that localised data is easier to manage and control, protection of that data from cyber-attacks and data thieves in localised environments might be more difficult. At some point in the not-to-distant future, regulators need to come to grips with the cloud.

Level 13, The Gate, PO Box 75850, Dubai, UAE
Telephone: +971 (0)4 362 1500
Fax: +971 (0)4 362 0801

Cyber Supervision

While I have focused on the positives of digital transformation in the sector, and the benefits it can present to both the firm and their consumers, **there are definitely threats too.** The financial and reputational risks resulting from cyber-attacks and incidents are one of the biggest threats to the sector. This concern is understandable given the surge in high-profile cyber incidents in 2017 and 2018.

One of the key challenges for financial services institutions is being able to keep pace with cyber-attacks, coupled with the relentlessness and, often, ruthlessness of the attacks. Many can be over-confident in their ability to withstand an attack. The more complex and sophisticated cyber controls become, the more sophisticated cyber criminals become. Therefore, even the best defences cannot eliminate completely the risk of a successful cyber-attack. Consequently, though guarding against a cyber incident is a primary objective it is equally, if not more, important for a firm to make sure it is prepared to respond to and recover from an incident. Put another way, we expect Firms to focus on ensuring they can be resilient to a successful cyber incident.

So what can financial services institutions do? Clearly, the priority is to prevent a cyber-incident from occurring but it seems to be a question of <u>when</u> – rather than <u>if</u> – a breach will occur. It is therefore vital to have an effective response strategy to ensure that attacks can be quickly and effectively detected, analysed and responded. Knowledge sharing and industry collaboration is also important to stay ahead of the curve. Similar to their effectiveness in fighting financial crime, public / private partnerships are critical to cyber prevention and response strategies.

At the DFSA, we are increasing our focus on cyber risk. In particular, we are focusing on firms' resilience to cyber incidents. The DFSA is in the process of launching the region's first regulator-hosted cyber threat intelligence platform. The platform will be available to all companies (regulated and non-regulated) operating in or from the DIFC, and the objective of the platform is to facilitate the development of a community of information sharing. The DFSA will host the platform on its infrastructure and will outsource management and enrichment of the platform to a third party cyber security specialist firm.

In the past week, the DFSA launched an online reporting mechanism for Authorised Firms to report cyber incidents to the DFSA. The goal of the mechanism is to provide DFSA with consistent reporting of incidents, to make clear to Firms what information the DFSA expects to receive, and

Dubai Financial Services Authority

provide DFSA timely information with which to assess the potential for systemic impact. Where DFSA deems it necessary, the threat intelligence platform we will alert other companies of the threat.

Despite challenging macro-economic and global conditions, we feel incredibly positive about the future and development of the financial services industry in Dubai, the UAE and the region. There is a lot of fantastic work stimulating and encouraging innovation and technology, which is very much the future of finance. We look forward to playing an active part in this.

Thank you.