

VIRTUAL FINANCIAL ASSETS RULEBOOK

CHAPTER 3

VIRTUAL FINANCIAL ASSETS RULES FOR VFA SERVICE PROVIDERS

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REVISIONS LOG

VERSION	DATE ISSUED	DETAILS
1.00	25 FEBRUARY 2019	CHAPTER 3 OF THE VFA RULEBOOK ISSUED
1.01	21 MAY 2019	AMENDMENT TO SUB-SECTION 2, SECTION 3, TITLE 3 OF THIS RULEBOOK
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1.03	10 DECEMBER 2019	VARIOUS AMENDMENTS TO CHAPTER 3 OF THE VFA RULEBOOK

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Title 1 General Scope and High Level Principles

Section 1 **Scope and Application**

- R3-1.1.1 This Chapter shall apply to VFA Service Providers licensed in terms of the Virtual Financial Assets Act ('the Act') and Applicants seeking Licensing as VFA Service Providers under the Act, as applicable.
- R3-1.1.2 This Title outlines the high level principles which should guide VFA Service Providers in the provision of their VFA service in or from within Malta.
- R3-1.1.3 Title 2 of this Chapter outlines the Licensing requirements and the respective authorisation process for VFA Service Providers.
- R3-1.1.4 Title 3 of this Chapter outlines the ongoing obligations which VFA Services Licence Holders must adhere to.
- R3-1.1.5 Title 4 of this Chapter provides for enforcement and sanctions in the event of misconduct by VFA Service Providers.

Section 2 High Level Principles

- R3-1.2.1 VFA Service Providers shall act in an ethical manner taking into consideration the best interests of their clients and the integrity of Malta's financial system.
- R3-1.2.2 VFA Service Providers shall act honestly, fairly and professionally and shall comply with the relevant provisions of the Act, the VFA Regulations issued thereunder, and these Rules as well as with other relevant legal and regulatory requirements.
- R3-1.2.3 VFA Service Providers shall co-operate with the MFSA in an open and honest manner and shall provide the Authority with any information it may require.
- R3-1.2.4 In complying with R3-1.2.1, VFA Service Providers and their related Functionaries shall:
- i. make reference to, and where applicable comply with, the applicable Maltese laws, VFA Regulations and the Rules issued thereunder as well as any Guidance Notes which may be issued by the MFSA or other relevant body to assist the said persons in complying with their legal and regulatory obligations.
 - ii. cooperate in an open and honest manner with the MFSA and any other relevant regulatory authorities, including the FIAU; and

- iii. take due account and, where applicable, comply with any relevant EU legislation as well as any Guidance Notes/Statements/Industry Best Practices which may be issued by international standard setting bodies including any Guidelines or Guidance Notes issued by the FIAU.

Title 2 Authorisation Requirements of VFA Service Providers

Section 1 General

Sub-Section 1 Scope and Application

R3-2.1.1.1 This Title identifies the Licensing requirements for Applicants wishing to be licensed as VFA Service Providers under the Act, and the applicable Licensing process.

R3-2.1.1.2 This section sets out the Licensing requirement for VFA Service Providers.

Sub-Section 2 Licensing Requirement for VFA services

R3-2.1.2.1 Pursuant to Article 13 of the Act, a person providing, or holding itself out as providing, a VFA service in or from within Malta without being in possession of a valid licence granted under the Act, issued by the MFSA, shall be in breach of the Act.

R3-2.1.2.2 A person wishing to provide a VFA service shall be required to apply for a VFA Services Licence in accordance with the Act and the requirements set out in this Title.

R3-2.1.2.3 Provided that the Licensing requirement under R3-2.1.2.2 shall apply only insofar as such service is not exempt under the VFA Regulations.

R3-2.1.2.4 The four classes of VFA Services Licences are the following:

R3-2.1.2.4.1 **Class 1**
Licence holders authorised to receive and transmit orders and/ or provide investment advice in relation to one or more virtual financial assets and/ or the placing of virtual financial assets. Class 1 Licence Holders are not authorised to hold or control clients' assets or money.

R3-2.1.2.4.2 **Class 2**
Licence holders authorised to provide any VFA service but not to operate a VFA exchange or deal for their own account. Class 2 Licence Holders may hold or control clients' assets or money in conjunction with the provision of a VFA Service.

R3-2.1.2.4.3 **Class 3**
Licence holders authorised to provide any VFA service but not to operate a VFA exchange. Class 3 Licence Holders may hold or control clients' assets or money in conjunction with the provision of a VFA Service.

R3-2.1.2.4.4 **Class 4**
Licence holders authorised to provide any VFA service. Class 4 Licence Holders may hold or control clients' assets or money in conjunction with the provision of a VFA Service.

R3-2.1.2.5 Pursuant to Regulation 8 of the VFA Regulations, the MFSA has the discretion to determine into which category an Applicant shall fall.

R3-2.1.2.6 A person wishing to be licensed to provide a VFA service shall be a legal person established in Malta.

Sub-Section 3 VFA Agent Requirement

R3-2.1.3.1 A person seeking licensing under the Act in order to provide a VFA service shall appoint a VFA Agent registered with the MFSA in terms of Chapter 1 of these Rules and having the responsibilities outlined therein.

R3-2.1.3.2 Where an Applicant appoints more than one VFA Agent, the Applicant shall establish how responsibility is to be allocated and inform the MFSA, in writing, of the respective allocations so made.

R3-2.1.3.3 The Applicant shall ensure that all communications, meetings, notifications and submissions to the MFSA are made through its VFA Agent.

R3-2.1.3.4 The Applicant shall, at all times, collaborate in an open and honest manner with its VFA Agent and shall provide the VFA Agent with any information it may require particularly with regards to the fitness and properness assessment that the VFA Agent must conduct in respect to the Applicant.

R3-2.1.3.5 The Applicant may appoint its VFA Agent to undertake the compliance function in accordance with Sub-Section 4 of Section 1 of Title 3 of this Chapter.

Sub-Section 4 Systems Auditor Requirement

R3-2.1.4.1 General Requirements

R3-2.1.4.1.1 Where an Applicant has Innovative Technology Arrangement/s in place as part of its operations, or operates a technological infrastructure which interacts with an Innovative Technology Arrangement in some way or form, the Authority shall require an Applicant to appoint a Systems Auditor.

- R3-2.1.4.1.2 The MFSA may object to the proposed appointment or replacement of a Systems Auditor and may require such additional information as it may consider appropriate.
- R3-2.1.4.1.3 The Applicant shall make available to its Systems Auditor the information and explanations it needs to discharge its responsibilities as a Systems Auditor and in order to meet the MFSA's requirements.
- R3-2.1.4.1.4 The MFSA may at its discretion, at any time, require a review or audit on the characteristics of the Applicant's systems by another Systems Auditor.
- R3-2.1.4.1.5 At application stage, an Applicant shall ensure that its Systems Auditor prepares a Systems Audit Report in line with the MDIA's guidelines, as well as any guidelines on cyber security issued by the Authority. Such report shall be required to be submitted to the MFSA and a copy thereof to the MDIA.
- R3-2.1.4.2 *Letter of Engagement*
- R3-2.1.4.2.1 The Applicant shall obtain from its Systems Auditor a signed letter of engagement defining clearly the extent of the Systems Auditor's responsibilities and the terms of its appointment. The Applicant shall confirm in writing to its Systems Auditor its agreement to the terms in the letter of engagement.
- R3-2.1.4.2.2 The letter of engagement shall, at least, include terms requiring the Systems Auditor:
- i. to review and audit the Applicant's systems in line with the MDIA's guidelines, as well as any guidelines on cyber security issued by the Authority;
 - ii. to provide such information or verification to the MFSA as the MFSA may request;
 - iii. to afford another Systems Auditor any assistance as it may require;
 - iv. to vacate its office if, for any reason, it becomes disqualified to act as Systems Auditor;
 - v. to notify the MFSA if it resigns, is removed or not reappointed and of the reasons for its ceasing to hold office. The Systems Auditor shall also be required to advise the MFSA if there are matters it considers should be brought to the attention of the MFSA; and
 - vi. to report immediately to the MFSA any fact or decision of which it becomes aware in its capacity as Systems Auditor of the Applicant or VFA Service Provider, as applicable, which constitutes or is likely to

constitute a material breach of the applicable legal and regulatory requirements in or under the Act.

Sub-Section 5 IT Auditor Requirement

R3-2.1.5.1 Where an Applicant does not have an Innovative Technology Arrangement in place as part of its operations, or operate a technological infrastructure which interacts with an Innovative Technology Arrangement in some way or form, the Applicant shall be required to appoint an IT Auditor. In such case, Rules R3-2.1.4.1.2 to R3-2.1.4.1.5 and R3-2.1.4.2 shall apply *mutatis mutandis*.

R3-2.1.5.2 The IT Auditor shall be responsible for reviewing and auditing the Applicant's systems in line with any internationally and nationally recognised standards as well as any guidelines issued by the Authority.

R3-2.1.5.3 At application stage, an Applicant shall ensure that its IT Auditor prepares an IT Audit Report in line with any internationally and nationally recognised standards as well as any guidelines issued by the Authority. Such report shall be required to be submitted to the MFSA.

Provided that the IT Audit Report shall include a confirmation from the IT Auditor that the Applicant does not have an Innovative Technology Arrangement in place as part of its operations or operate a technological infrastructure which interacts with an Innovative Technology Arrangement in some way or form.

Sub-Section 6 Live Audit Log

R3-2.1.6.1 The Applicant shall establish, and have at all times in place, a Live Audit Log in line with the MDIA's Forensic Node Guidelines, which shall apply *mutatis mutandis*, and shall fall within the scope of the Systems Audit, in terms of Sub-Section 4, or the IT Audit, in terms of Sub-Section 5, as the case may be.

Furthermore, the Applicant shall also appoint a person with the necessary seniority, skills, knowledge and experience to ensure that any request for information regarding legal compliance and the operational behaviour of the system can be acted upon satisfactorily. Such person shall assume responsibilities similar to those of a Technical Administrator, as referred to in the MDIA's Forensic Node Guidelines, which shall apply *mutatis mutandis*.

Provided that where an Applicant:

- i. does not have an Innovative Technology in place; or
- ii. whereas it has an Innovative Technology Arrangement in place, same has not been certified by the MDIA

such person shall not be required to be registered with the MDIA as a Technical Administrator.

R3-2.1.6.2 The Applicant shall notify the MFSA prior to the appointment or replacement of the person referred to in R3-2.1.6.1.

Provided that the MFSA may object to the proposed appointment or replacement and to require such additional information as it may consider appropriate.

Section 2 Licensing as a VFA Service Provider

Sub-Section 1 Scope and Application

R3-2.2.1.1 This Section stipulates the considerations taken into account by the Authority when assessing an application for the Licensing of a VFA Service Provider, as well as the underlying considerations of the fitness and properness assessment.

Sub-Section 2 Licensing Considerations

R3-2.2.2.1 When considering whether to issue a licence to operate to an Applicant, the Authority shall, *inter alia*, have regard to:

- i. the protection of investors and the general public;
- ii. the protection of the reputation of Malta taking into account Malta's international commitments;
- iii. the promotion of innovation, competition and choice; and
- iv. the reputation and suitability of the Applicant and all other parties connected with the Applicant.

R3-2.2.2.2 Pursuant to the considerations outlined in R3-2.2.2.1, and in accordance with Article 15 of the Act, the Authority may licence an Applicant as a VFA Service Provider, subject to the Applicant being a fit and proper person.

Provided that the Applicant shall be compliant with all application requirements determined under relevant provisions of the Act, and these Rules and the VFA Regulations issued thereunder, as applicable.

R3-2.2.2.3 The onus of providing sufficient assurance to the Authority that the person is a fit and proper person to provide the VFA services concerned rests with the Applicant and its VFA Agent.

R3-2.2.2.4 Notwithstanding R3-2.2.2.3, the Authority shall, as part of the assessment process, avail itself of any additional information which may be available to it. Such information may include information which was not provided by the Applicant.

Sub-Section 3 Fitness and Properness

R3-2.2.3.1 General

R3-2.2.3.1.1 Applicants seeking authorisation under the Act shall be required to meet the fitness and properness requirements specified in these Rules both during authorisation stage as well as on an ongoing basis thereafter.

R3-2.2.3.1.2 Pursuant to R3-2.2.3.1.1, in assessing whether a person is a fit and proper person, the Authority shall require that all the following three criteria are satisfied:

- i. Integrity, as further specified in R3-2.2.3.2;
- ii. Competence, as further specified in R3-2.2.3.3; and
- iii. Solvency, as further specified in R3-2.2.3.4.

R3-2.2.3.1.3 The fitness and properness assessment shall be applicable to every (i) person that has a qualifying holding in the Applicant, (ii) beneficial owner, (iii) member of the Board of Administration of the Applicant, (iv) Senior Manager, (v) MLRO, (vi) Compliance Officer and any other person which the Authority may deem necessary.

R3-2.2.3.2 Integrity

R3-2.2.3.2.1 The Applicant and the persons referred to in R3-2.2.3.1.3 shall demonstrate and provide reasonable assurance to the satisfaction of the Authority that they are of good repute as well as of their intentions to act in an honest and trustworthy manner.

R3-2.2.3.3 Competence

R3-2.2.3.3.1 The Applicant and persons referred to in R3-2.2.3.1.3 shall demonstrate and provide reasonable assurance to the satisfaction of the Authority, both collectively and individually, that they have an acceptable level of knowledge, professional expertise and experience.

R3-2.2.3.3.2 The Applicant shall also demonstrate and provide reasonable assurance to the satisfaction of the Authority that adequate systems and controls are in place for the provision of the VFA service/s they intend to offer.

R3-2.2.3.3.3 The persons referred to in R3-2.2.3.1.3 shall also demonstrate and provide reasonable assurance to the satisfaction of the Authority that they have sufficient competence in terms of qualifications, experience and skills as well as that they are capable of committing sufficient time to effectively carry out their particular activities or functions within the Applicant's proposed structure.

R3-2.2.3.3.4 The Authority shall schedule a mandatory interview with the proposed Compliance Officers and MLROs, and, where it deems it necessary, conduct any further assessment.

Provided that the Authority may also, at its discretion, require an interview with any other proposed person referred to in R3-2.2.3.1.3 as it may deem necessary.

Provided further that the Authority may, at its discretion, request that an individual proposed as Compliance Officer and, or MLRO complete a course, either at pre-licensing or post-licensing stage.

Provided further that Compliance Officers, MLROs and, where applicable, other proposed persons referred to in R3-2.2.3.1.3 shall be deemed competent by the Authority only where such persons satisfy all the aforementioned requirements.

R3-2.2.3.4 *Solvency*

R3-2.2.3.4.1 The Applicant shall demonstrate and provide reasonable assurance to the satisfaction of the Authority that it is financially sound, that proper financial control is ensured and management of liquidity will be applied in the course of the provision of the proposed VFA service/s.

R3-2.2.3.4.2 The Applicant shall maintain an amount equal to the initial capital required for their authorisation and as permanent minimum capital at all times the amount specified in R3-2.2.3.4.3.

R3-2.2.3.4.3 The initial capital requirements applicable to each respective class of VFA Service Providers are indicated in Table R3-1.

TABLE R3-1: INITIAL CAPITAL REQUIREMENTS FOR VFA SERVICE PROVIDERS

VFA Services Licence	Initial Capital Requirement (EUR)		
Class 1	i.	50,000	OR
	ii.	25,000 and PII	
Class 2		125,000	
Class 3		730,000	
Class 4		730,000	

- R3-2.2.3.4.4 The Applicant should demonstrate and provide reasonable assurance to the satisfaction of the Authority that (i) it has sufficient financial resources to remain financially viable and to carry out its services through economic cycles; or (ii) to enable an orderly wind-down without causing undue economic harm to their clients or to the stability of the markets they operate in.
- R3-2.2.3.4.5 Further to R3-2.2.3.4.2, the Applicant should demonstrate and provide reasonable assurance to the satisfaction of the Authority that it shall have sufficient financial resources, at all times, to meet their Capital Requirements in accordance with Title 3 of this Chapter.

Section 3 The Licensing Processes

Sub-Section 1 Scope and Application

- R3-2.3.1.1 This Section outlines the Licensing process applicable to VFA Service Providers.

Sub-Section 2 General

- R3-2.3.2.1 Applicants or VFA Service Providers shall submit any notifications and/or Authorisation documents, as applicable, and in accordance with this Section, to the Authority through the [Authority's Licence Holder Portal \('LH Portal'\)](#). Any correspondence in relation to an application should be made through the chat box function therein. Any documentation requested in original should be submitted to the Authority in writing.
- R3-2.3.2.2 The MFSA shall base its decision as to whether an Applicant has met the required standards, on the basis of the discussions, information provided by the proposed person/s, and any other information that ought to have been disclosed by the proposed person/s. The MFSA shall not be liable in damages for any acts or omissions on the part of the proposed person/s.

Sub-Section 3 The Application Process for VFA Service Providers

R3-2.3.3.1 General

- R3-2.3.3.1.1 The application process consists of three phases, (i) phase one being the preparatory phase, (ii) phase two being the pre-licensing phase and (iii) phase three being the post-licensing / pre-commencement of business phase.

R3-2.3.3.2 Preparatory Phase

- R3-2.3.3.2.1 The Applicant shall notify the Authority in writing and via email through VFA@mfsa.mt, through its VFA Agent, of its intention to apply for a VFA Services Licence.
- R3-2.3.3.2.2 Pursuant to R3-2.3.3.2.1, the statement of intent shall include:
- i. a comprehensive written description of the proposed structure;
 - ii. the VFA Service/s for which Licensing is being sought identifying the persons proposed to hold key positions thereto; and
 - iii. a legal opinion that the proposed activity does not fall within the scope of traditional financial services legislation.
- R3-2.3.3.2.3 The Authority, upon receipt of the aforementioned statement of intent, shall schedule a preliminary meeting with the Applicant. Such a meeting is mandatory during this phase of the application process.
- R3-2.3.3.2.4 The Applicant shall, by not later than 60 days from the date of the preliminary meeting, submit an application form with any supporting documentation as specified therein.
- Provided that the Authority may, under exceptional circumstances, extend the aforementioned period should the Applicant provide justifiable reasons for the said extension and specify that no material changes to the proposed application have been made since the preliminary meeting.
- R3-2.3.3.2.5 Applicants shall also pay the applicable non-refundable application fee to the Authority, in accordance with the VFA Regulations, when submitting the application form.
- R3-2.3.3.2.6 The Authority shall not initiate the review of any application which is not complete.
- Provided that the submission of the application shall be considered complete only upon receipt of all required documentation as well as the verification that the respective application fees have been submitted to the Authority.
- R3-2.3.3.3 *Pre – Licensing Phase*
- R3-2.3.3.3.1 The Authority shall, upon submission of a complete application, initiate the review of the application and the supporting documentation.
- R3-2.3.3.3.2 The Applicant and its VFA Agent shall inform the Authority of any changes required to the application form as soon as possible.

R3-2.3.3.3.3 The Authority shall, once it is satisfied with the information set out in the application documentation and the completion of the fitness and properness assessment, issue an 'in principle Approval', which shall be valid for a period of three months from the date of the issue thereof.

R3-2.3.3.3.4 Pursuant to R3-2.3.3.3.3, Applicants shall, during the three months:

- i. finalise any outstanding issues raised during the application process;
- ii. finalise any pre-Licensing conditions as determined by the Authority in the in-principle Approval; and
- iii. submit the original copies of the final application form together with all supporting documentation.

R3-2.3.3.3.5 Upon satisfaction of the requirements in R3-2.3.3.3.4, a VFA Services Licence shall be issued by the Authority.

R3-2.3.3.4 *Post-Licensing & Pre-Commencement of Business*

R3-2.3.3.4.1 Licence Holders may be required to satisfy, within set timeframes, a number of post-licensing matters, as determined by the Authority, prior to the commencement of business.

R3-2.3.3.4.2 The MFSA may vary or revoke any condition of a Licence as well as impose new conditions thereto.

R3-2.3.3.4.3 The Authority shall have the power to cancel the Licence granted to a VFA Service Provider should it fail to satisfy the post-licensing matters within the set timeframes as stipulated by the Authority.

R3-2.3.3.4.4 The Licence Holder shall commence its VFA Services business within twelve months of the date of issue of the VFA Services Licence.

Provided that, if for any reason the Licence Holder is not in a position to comply with this condition, it shall notify the MFSA in writing setting out the reason/s for such a delay together with an updated business plan indicating the proposed date of commencement of business. On the basis of the information provided and the circumstances of the case, the MFSA may decide to suspend or cancel the Licence in accordance with the relevant provisions of the Act.

R3-2.3.3.4.5 The Licence Holder shall also be required to adhere to the applicable Titles of this Rulebook upon being granted the VFA Services Licence.

Sub-Section 4 The Ongoing Licensing Obligations for VFA Service Providers

R3-2.3.4.1 *Revision of a Licence*

R3-2.3.4.1.1 Licence Holders wishing to amend or extend their Licence, shall notify the Authority of their intention to do so prior to effecting the change.

Provided that should a Licence Holder wish to change its VFA Services Licence Class, such Licence Holder shall be required to appoint a VFA Agent and an application for revision shall be made through the VFA Agent. In such case, Rules R3-2.1.3.2 to R3-2.1.3.4 shall apply *mutatis mutandis*.

The Licence Holder shall also include in the aforementioned notification a comprehensive description of the proposed revision.

R3-2.3.4.1.2 The Authority, upon receipt of the aforementioned statement of intent, shall schedule a preliminary meeting, with the Licence Holder.

R3-2.3.4.1.3 The Licence Holder shall, by not later than 60 days of the date of the preliminary meeting, submit, through the chat box function within the [Authority's LH Portal](#), detail of the variation being requested, outlining the changes required to the latest application form submitted.

R3-2.3.4.1.4 The Licence Holder shall include in the aforementioned request the following documentation:

- i. Administrators' resolution approving the changes;
- ii. a revised business plan; and
- iii. revised financial projections.

Provided that the Authority may, under exceptional circumstances, extend the aforementioned period should the Licence Holder provide justifiable reasons for the said extension and that no material changes to the revision have been made since the preliminary meeting.

R3-2.3.4.1.5 Licence Holders shall also pay a nominal revision fee of EUR 1,000 when submitting the request to amend the application form to the Authority.

Provided that should the Licence Holder wish to change its VFA Services Licence Class, the Licence Holder shall pay the full Application Fee in accordance with the VFA Regulations.

R3-2.3.4.1.6 The Authority shall not initiate the review of applications which are not complete.

Provided that for purposes of applications to amend an application form shall only be considered complete upon receipt of all required documentation as

well as the verification that the respective revision fee has been submitted to the Authority.

R3-2.3.4.1.7 The Authority shall, once it is satisfied with the information received for purposes of amending an application form and, where applicable, the completion of the fitness and properness assessment, issue an 'in principle Approval' for the issuance of the revised VFA Services Licence, which shall be valid for a period of three months from the date of the issue thereof.

R3-2.3.4.1.8 The Authority shall issue the revised VFA Services Licence to the Licence Holder, upon satisfaction of the requirements in this sub-section.

R3-2.3.4.2 *Change in Unitholding and Beneficial Ownership of Licence Holders*

R3-2.3.4.2.1 A Licence Holder shall notify the Authority of any changes to the Unitholding structure immediately upon becoming aware of such changes.

Provided that any change in the Licence Holder's Qualifying Holding or Beneficial Ownership structure shall require the Authority's prior approval.

R3-2.3.4.2.2 Pursuant to R3-2.3.4.2.1, the notification shall also clearly indicate the Qualifying Holder/s as well as the Beneficial Owner/s following the proposed change in the Licence Holder's structure.

R3-2.3.4.2.3 Pursuant to the proviso to R3-2.3.4.2.1, the Authority shall approve a Qualifying Holder and/or a Beneficial Owner only if such person satisfies the 'fitness and properness' assessment.

R3-2.3.4.3 *Provision of VFA Services in Other Jurisdictions*

R3-2.3.4.3.1 Where a Licence Holder wishes to provide its services in other jurisdictions, it shall notify the Authority of its intention in writing prior to the provision of, or to holding itself out as providing, any VFA service in another jurisdiction.

Provided that Licence Holders shall at all times abide by the applicable laws when operating in another jurisdiction.

R3-2.3.4.3.2 Licence Holders should also include within the aforementioned notification the intended jurisdiction/s and the VFA service/s intended to be offered thereto.

R3-2.3.4.3.3 Licence holders shall also carry out an internal assessment so as to determine whether the laws of the jurisdiction/s allow for the provision of such services prior to submitting the statement of intent to the Authority. The said statement shall include a confirmation in this regard.

R3-2.3.4.4 *Other Matters requiring Approval or Notifications*

R3-2.3.4.4.1 The Licence Holder shall notify the MFSA in writing of:

- i. a change of address and/or any changes to contact details as soon as it becomes aware.
- ii. any proposed acquisitions or disposals of Units which fall within the disclosure provisions of the Act – immediately upon becoming aware of the proposed acquisition or disposal. It should be noted that the MFSA has the right to object to such an acquisition.
- iii. any proposed material change to its business at least one month before the change is to take effect.
- iv. any evidence of fraud or dishonesty by a member of the Licence Holder's staff immediately upon becoming aware of the matter.
- v. any evidence of hacking, fraud or other serious malpractice suffered by the Licence Holder.
- vi. a decision to make a material claim on its professional indemnity insurance or on any other insurance policy held in relation to its business. The notification should be provided as soon as the decision is taken.
- vii. any actual or intended legal proceedings of a material nature by or against the Licence Holder immediately after the decision has been taken or on becoming aware of the matter.
- viii. any material changes in the information supplied to the MFSA – immediately upon becoming aware of the matter.
- ix. any other material information concerning the Licence Holder, its business or its staff in Malta or abroad – immediately upon becoming aware of the matter.
- x. any breach of these Rules, the Act or the VFA Regulations issued thereunder, as soon as the Licence Holder becomes aware of the breach.
- xi. any decision to make an application to a Regulator abroad to undertake any form of activity outside Malta.
- xii. the appointment of any persons, whether Administrators, Senior Managers or other employees are engaged in any of the following activities:

- a. portfolio management; or
- b. investment advice.

Provided that the Authority may, at its discretion, object to the proposed engagement or acquisition referred to in (xii) and (xiii) above.

Notwithstanding the above, the MFSA shall be notified where any other MFSA notification is required in terms of the Rules.

R3-2.3.4.4.2 The Licence Holder shall obtain the Written Consent of the MFSA before:

- i. making a change to its registered name, business or trade name, as applicable.
- ii. implementing material changes to its business at least one month before the change is to take effect, notwithstanding whether the proposed material change/s require authorisation or otherwise.

Where a variation of the VFA Services Licence or a new authorisation is required, the new business shall not commence until it has been approved by the MFSA.

- iii. making any change to its capital or the rights of its Unitholders.
- iv. acquiring 10 per cent or more of the voting rights in another entity.
- v. agreeing to sell or merge the whole or any part of its undertaking.
- vi. the appointment of an Administrator or Senior Manager responsible for the VFA Services business of the Licence Holder or of the Licence Holder's Compliance Officer and/or MLRO or of the Licence Holder's Risk Manager, where applicable.
- vii. the change in the responsibilities of an Administrator or Senior Manager. A change in the responsibilities of an Administrator or Senior Manager should only be notified to the MFSA when such a change is material, which shall include a change in the status or seniority of the person concerned (upwards or downwards).

Notwithstanding the above, the consent of the MFSA shall be required where any other MFSA approval is required in terms of the Rules.

R3-2.3.4.5 *Fees*

R3-2.3.4.5.1 The Licence Holder shall promptly pay all amounts due to the MFSA.

R3-2.3.4.5.2 The Annual Supervisory Fee shall be payable by the Licence holder, on the day of submission of the annual audited financial statements.

Licence Holders, upon authorisation, shall be required to pay the minimum annual supervisory fee for the first year of operation upon receipt of the Licence. The fee payable shall be proportionate to the period remaining between the date of granting of the Licence and the date of the submission of the annual audited financial statements.

Sub-Section 5 Voluntary Suspension of VFA Services Licence

R3-2.3.5.1 A Licence Holder may request the Authority to voluntarily suspend its VFA Services Licence for a period of up to 6 months. Licence Holders are required to adhere to all applicable Rules during the period of suspension.

Provided that the Authority may exempt the Licence Holder from maintaining its Capital Requirements in accordance with Title 3 of this Chapter during the period of suspension.

Provided further that this Rule shall only apply if the Licence Holder does not have clients and will not on-board new clients during the suspension period.

R3-2.3.5.2 Licence Holders intending to suspend their Licence voluntarily shall inform the MFSA of their intention to do so promptly and by not later than five working days after such decision was taken.

R3-2.3.5.3 Notwithstanding the notification submitted in accordance with R3-2.3.5.2, Licence Holders shall submit a formal request for the approval of the voluntary suspension to the MFSA. The request should also include a detailed justification as to why the suspension is required, and the efforts being made by the Licence Holder to continue its business.

R3-2.3.5.4 The Authority shall proceed with the internal process to approve the voluntary suspension of the Licence upon submission of an Administrators' resolution confirming that the Licence Holder:

- i. intends to voluntarily suspend its VFA Services Licence, subject to the Authority's approval and once the necessary formalities are finalised;
- ii. does not have any clients and will not on board new clients during the suspension period;

and any other documentation as may be determined appropriate by the Authority.

- R3-2.3.5.5 In the event of a voluntary suspension being approved by the Authority, a public notice regarding the suspension of the Licence shall be published on the MFSA's website.
- R3-2.3.5.6 The Licence Holder may request an extension of the suspension period subject that adequate and satisfactory justification is provided thereto. The request should also include a detailed justification as to why the suspension is required, and the efforts being made by the Licence Holder to continue with its business.
- R3-2.3.5.7 Notwithstanding the notification submitted in accordance with R3-2.3.5.6, the Licence Holder shall have to resubmit to the Authority a resolution from its Board of Administration confirming the Licence Holder's intention to extend the voluntary suspension period.
- R3-2.3.5.8 Subject that the extension of the suspension of Licence is approved by the Authority, a public notice regarding the suspension of the Licence will be re-issued on the MFSA website.

Sub-Section 6 Cessation Process for VFA Service Providers

- R3-2.3.6.1 Licence Holders ceasing their VFA Services business and thus intending to surrender their VFA Services Licence should inform the MFSA of their intention to do so promptly and by not later than five working days after such decision was taken.
- Provided that the Licence Holder shall also provide due notice to its clients that it intends to surrender its VFA Services Licence immediately upon becoming aware of such intention.
- R3-2.3.6.2 Notwithstanding the notification submitted in accordance with R3-2.3.6.1, Licence Holders shall have to submit a formal request to the MFSA for the approval of the surrender of the VFA Services Licence.
- R3-2.3.6.3 The Authority shall proceed with the internal process to approve the surrender of the VFA Services Licence upon submission of the following documentation by the Licence Holder and any other documentation, as may be determined appropriate by the Authority:
- i. an Administrators' Resolution confirming the Licence Holder's intention to surrender its VFA Services Licence under the Act, subject to the Authority's approval and once the necessary formalities are finalised;
 - ii. a confirmation that no litigation is pending which arises out of any event that occurred during the authorisation of the Licence Holder;

- iii. a declaration that there are no pending complaints against the Licence Holder;
- iv. a confirmation that the Licence Holder will remove from all letterheads, and any other stationery, any reference to being authorised by the Authority;
- v. a confirmation that the Licence Holder has informed its Auditor and insurer of its intention to surrender its VFA Services Licence;
- vi. a confirmation that due notice has been given to its clients of its intention to surrender its VFA Services Licence, in terms of the proviso to R3-2.3.6.1;
- vii. a confirmation that each client has specifically consented to the transfer of that client's business to another appropriately licensed VFA Service Provider, if appropriate; and
- viii. a confirmation from the Licence Holder's Auditor specifying the date by when all business and obligations arising from the Licence Holder's activities related to its VFA Services Licence have been settled.

R3-2.3.6.4 The Authority may request the Licence Holder to delay the surrender of its VFA Services Licence or the cessation of its business should, at any stage of the process, it determine that such delay is required in order to ensure investor protection and market integrity.

R3-2.3.6.5 Once all the requirements listed under this Sub-Section are satisfied, the internal process for the approval of the surrender of the VFA Services Licence will commence. Where the Authority decides to approve the surrender, the decision will be communicated to the Licence Holder which will cease to be licensed upon returning its original VFA Services Licence to the MFSA. Moreover, following the Authority's approval of the surrender, unless arrangements are made for the winding up of the Licence Holder, a certified true copy of the Constitutional Document of the Licence Holder duly amended to remove all references to VFA Services activity and, where appropriate, to change the name of the Licence Holder shall be submitted to the Authority.

Provided that the Authority shall not proceed with the internal process to approve the surrender of the VFA Services Licence until the VFA Service Provider has paid all the application and/ or supervisory fees due to the Authority.

Section 4 Processes for Appointed Persons

Sub-Section 1 Scope and Application

R3-2.4.1.1 This Section shall apply to Applicants or Licence Holders proposing persons referred to in R3-2.2.3.1.3.

Sub-Section 2 Approval and Departure Process

R3-2.4.2.1 There are two processes relating to appointed persons, namely (i) the approval process and (ii) the departure process.

R3-2.4.2.2 Proposed persons shall submit any documentation to the Authority through the chat box function within the [Authority's LH Portal](#). Any documentation requested in original should be submitted to the Authority in writing.

R3-2.4.2.3 The MFSA shall use all the information provided by the proposed person, and any other information that ought to have been disclosed by the said person for the purposes of the processes referred to in R3-2.4.2.1. The MFSA shall not be liable in damages for any acts or omissions on the part of the proposed person.

Sub-Section 3 The Approval Process

R3-2.4.3.1 Proposed persons appointed or designated in relation to Applicants or Licence Holders, shall inform and apply for approval from the Authority prior to engaging in their proposed role.

R3-2.4.3.2 The Licence Holder or the Applicant, as applicable, shall submit to the Authority, as part of the fitness and properness assessment on the proposed person, the Personal Questionnaire Form. The Authority shall initiate the fitness and properness assessment upon submission of the complete form and supporting documentation as stipulated therein.

R3-2.4.3.3 The Authority may also require further information from the Licence Holder, the Applicant or the proposed person. For purposes of this Rule, the MFSA may *inter alia* conduct interviews and request any supporting documentation it may deem necessary.

R3-2.4.3.4 The Authority shall, as part of the assessment process, use information not provided by the proposed person, including *inter alia* publicly available information. The Authority shall also make reference to the overall organisational structure of the Applicant or Licence Holder.

R3-2.4.3.5 Where the proposed person is deemed to be fit and proper, the Authority shall issue its 'in-principle' approval to the appointment or designation of the person within the Applicant or Licence Holder, as applicable.

Provided that the Authority may also require the appointed or designated person to fulfil certain conditions within set timeframes. These conditions shall be indicated in the 'in principle' approval letter.

Sub-Section 4

The Departure Process

R3-2.4.4.1 The Licence Holder shall notify the Authority of the resignation or removal of any person referred to in R3-2.2.3.1.3 by not later than five working days from the effective resignation or departure date. The Licence Holder shall also provide to the Authority together with this notification, a written statement noting the reason/s for departure and the remedial measures being taken to satisfy the Licensing conditions as applicable. The notification should be submitted to the Authority through the chat box function of the [LH Portal](#). Any documentation requested in writing should be submitted to the Authority in original.

R3-2.4.4.2 The Licence Holder shall request the person referred to in R3-2.4.4.1, to provide to the Authority, (i) the reason for their departure and (ii) a written confirmation that such departure was not a consequence of any regulatory implications or to provide relevant details of any such regulatory implications, as appropriate.

Title 3 Ongoing Obligations for VFA Service Providers

Section 1 Organisational Requirements

Sub-Section 1 Scope and Application

R3-3.1.1.1 This Title provides the ongoing obligations for VFA Service Providers licensed under the Act.

R3-3.1.1.2 This Section applies to all VFA Service Providers falling within scope of these Rules except for R3-3.1.2.2.3 to R3-3.1.2.2.8, R3-3.1.2.3 and R3-3.1.2.4, which shall apply to Class 2, Class 3 and Class 4 VFA Service Providers only.

Sub-Section 2 Governance

R3-3.1.2.1 Governance Arrangements

R3-3.1.2.1.1 The Licence Holder's business shall be effectively directed or managed by at least two individuals in satisfaction of the 'dual control' principle. Such persons shall be of sufficiently good repute, possess sufficient knowledge and experience, commit sufficient time to perform their functions and be sufficiently experienced so as to ensure the sound and prudent management of the Licence Holder.

R3-3.1.2.1.2 The Licence Holder shall take reasonable steps to ensure continuity and regularity in the performance of its VFA Services. To this end, the Licence Holder shall employ appropriate and proportionate systems, resources and procedures.

R3-3.1.2.1.3 The Licence Holder shall:

- i. establish, implement and maintain decision-making procedures and an organisational structure which clearly and in a documented manner specifies reporting lines and allocates functions and responsibilities;
- ii. ensure that its relevant persons are aware of the procedures which must be followed for the proper discharge of their responsibilities;
- iii. establish, implement and maintain adequate internal control mechanisms designed to secure compliance with decisions and procedures at all levels of the Licence Holder;
- iv. employ personnel with the skills, knowledge and expertise necessary for the discharge of responsibilities allocated to them;

- v. establish, implement and maintain effective internal reporting and communication of information at all relevant levels of the Licence Holder;
- vi. maintain adequate and orderly records of its business and internal organisation; and
- vii. ensure that the performance of multiple functions by its relevant persons does not, and is not likely to, prevent those persons from discharging any particular function soundly, honestly and professionally.

For these purposes, the Licence Holder shall take into account the nature, scale and complexity of its business, and the nature and range of VFA services undertaken in the course of that business.

R3-3.1.2.1.4 The Licence Holder shall ensure that it has sound administrative and accounting procedures, internal control mechanisms, effective procedures for risk assessment, and effective control and safeguard arrangements for information processing systems.

R3-3.1.2.1.5 Without prejudice to R3-3.1.2.1.4, the Licence Holder shall establish, implement and maintain:

- i. systems and procedures that are adequate to safeguard the security, integrity and confidentiality of information, taking into account the nature of the information in question;
- ii. an adequate business continuity process in terms of R3-3.1.6.3. The business continuity policy shall be aimed at ensuring, in the case of an interruption to its systems and procedures, the preservation of essential data and functions and the maintenance of its VFA services, or, where that is not possible, the timely recovery of such data and functions and the timely resumption of its VFA Services;
- iii. accounting policies and procedures that enable it to deliver in a timely manner to the MFSA upon request, financial reports which reflect a true and fair view of its financial position and which comply with all applicable accounting standards and rules;
- iv. appropriate rules governing Personal Transactions by its officials and employees;
- v. sufficient records to be able to demonstrate compliance with the conditions of its VFA Services Licence and as required; and

- vi. adequate security arrangements including *inter alia* in relation to cyber security.
- R3-3.1.2.1.6 The Licence Holder shall have sound security mechanisms in place to guarantee the security and authentication of the means of transfer of information, minimise the risk of data corruption and unauthorised access and to prevent information leakage maintaining confidentiality of data at all times. For purposes of this Rule 'security' shall also include cyber security.
- R3-3.1.2.1.7 The Licence Holder shall monitor and, on a regular basis evaluate, the adequacy and effectiveness of its systems, internal control mechanisms and arrangements established in accordance with R3-3.1.2.1.1 and R3-3.1.2.1.3 and take appropriate measures to address any deficiencies.
- R3-3.1.2.1.8 Notwithstanding point (vi) of R3-3.1.2.1.5 and R3-3.1.2.1.6, a Licence Holder shall ensure that its cybersecurity architecture complies with any internationally and nationally recognised cyber security standards, any guidelines issued by the Authority and shall also be in line with the provisions of the GDPR.
- Provided that for purposes of this rule, the Licence Holder shall take into account the nature, scale and complexity of its business.
- R3-3.1.2.2 *Establishment of a Board of Administration*
- R3-3.1.2.2.1 Licence Holders shall comply with Article 24 of the Act.
- R3-3.1.2.2.2 Licence Holders shall also ensure that the Board of Administration define, approve and oversee:
- i. the organisation of the Licence Holder for the provision of VFA services, including the skills, knowledge and expertise required by personnel, the resources, the procedures and the arrangements for the provision of VFA services, taking into account the nature, scale and complexity of its business and all the requirements the firm has to comply with;
 - ii. a remuneration policy of persons involved in the provision of services to clients aiming to encourage responsible business conduct, fair treatment of clients as well as avoiding conflict of interest in the relationship with clients; and
 - iii. the internal capital adequacy assessment process in accordance with Sub-section 7, Section 3, Title 3 of this Chapter, if applicable.
- R3-3.1.2.2.3 The Board of Administration shall monitor and periodically assess the adequacy and implementation of the Licence Holder's strategic objectives in the provision of VFA services, the effectiveness of the Licence Holder's governance

arrangements and the adequacy of the policies relating to the provision of services to clients and take appropriate steps to address any deficiencies.

R3-3.1.2.2.4 The Licence Holder shall ensure that members of the Board of Administration have adequate access to information and documents which are needed to oversee and monitor management decision-making.

R3-3.1.2.2.5 The Licence Holder shall ensure that the members of its Board of Administration shall at all times be of sufficiently good repute, possess sufficient knowledge, skills and experience and commit sufficient time to perform their duties and be able to understand the Licence Holder's activities, including the main risks.

In this regard, the Licence Holder shall devote adequate human and financial resources to the induction and training of members of the Board of Administration.

R3-3.1.2.2.6 The Licence Holder shall ensure that each member of the Board of Administration shall act with honesty, integrity and independence of mind to effectively assess and challenge the decisions of the senior management where necessary and to effectively oversee and monitor management decision-making.

R3-3.1.2.2.7 The Licence Holder shall ensure that the Board of Administration defines, oversees and accounts for the implementation of the governance arrangements that ensure effective and prudent management of the Licence Holder, including the segregation of duties in the organisation and the prevention of conflicts of interest.

R3-3.1.2.2.8 The governance arrangements referred to above shall comply with the following principles:

- i. the Board of Administration shall have the overall responsibility for the Licence Holder and approve and oversee the implementation of the Licence Holder's strategic objectives, risk strategy and internal governance;
- ii. the Board of Administration shall ensure the integrity of the accounting and financial reporting systems, including financial and operational controls and compliance with the law and relevant standards;
- iii. the Board of Administration shall oversee the process of disclosure and communications;
- iv. the Board of Administration shall be responsible for providing effective oversight of senior management;

- v. the chairman of the Board of Administration in its supervisory function of the Licence Holder shall not exercise simultaneously the functions of a chief executive officer within the same Licence Holder, unless justified by the Licence Holder and authorised by the MFSA;
- vi. the Board of Administration shall monitor and periodically assess the effectiveness of the Licence Holder's governance arrangements and take appropriate steps to address any deficiencies; and
- vii. the Board of Administration shall ensure adequate systems and controls from an Information Technology point of view, including *inter alia* with respect to cyber-security.

R3-3.1.2.3 *Responsibility of Senior Management*

R3-3.1.2.3.1 When allocating functions internally, the Licence Holder shall ensure that senior management, and where appropriate, the supervisory function, are responsible for ensuring that the Licence Holder complies with its obligations under these Rules.

In particular, senior management and where appropriate, the supervisory function shall be required to assess and periodically review the effectiveness of the policies, arrangements and procedures put in place to comply with the obligations under these Rules and to take appropriate measures to address any deficiencies.

R3-3.1.2.3.2 For the purposes of this Section "supervisory function" means the function within a Licence Holder responsible for the supervision of its senior management.

R3-3.1.2.4 *Risk Consideration*

R3-3.1.2.4.1 The Board of Administration shall approve and periodically review the strategies and policies for taking up, managing, monitoring and mitigating the risks the Licence Holder is or might be exposed to, including those posed by the macroeconomic environment in which it operates in relation to the status of the business cycle.

R3-3.1.2.4.2 The Board of Administration shall devote sufficient time to consideration of risk issues. The Board of Administration shall be actively involved in and ensure that adequate resources are allocated to the management of all material risks. The Licence Holder shall establish reporting lines to the Board of Administration that cover all material risks and risk management policies and changes thereof.

- R3-3.1.2.4.3 The Board of Administration in its supervisory function and, where a risk committee has been established, the Risk Committee shall have adequate access to information on the risk situation of the Licence Holder and, if necessary and appropriate, to the risk management function and to external expert advice.
- R3-3.1.2.4.4 The Board of Administration in its supervisory function and, where one has been established, the Risk Committee shall determine the nature, the amount, the format, and the frequency of the information on risk which it is to receive.
- R3-3.1.2.4.5 The Licence Holder shall have in place adequate risk management processes and internal control mechanisms, including sound reporting and accounting procedures in order to identify, measure, monitor and control transactions with companies within their group appropriately. The Licence Holder shall report to the MFSA any significant transactions with those entities.

Sub-Section 3 Risk Management

R3-3.1.3.1 Policies and Procedures

- R3-3.1.3.1.1 The Licence Holder shall take the following actions with a view to managing its risks:
- i. establish, implement and maintain adequate risk management policies and procedures, which identify risks relating to the Licence Holder's activities, processes and systems, and where appropriate, set the level of risk tolerated by the Licence Holder;
 - ii. adopt effective arrangements, processes and mechanisms to manage the risks relating to the Licence Holder's activities, processes and systems, in light of that level of risk tolerance;
 - iii. monitor the following:
 - a. the adequacy and effectiveness of the Licence Holder's risk management policies and procedures;
 - b. the level of compliance by the Licence Holder and its relevant persons with the arrangements, processes and mechanisms adopted in accordance with point (ii) above; and
 - c. the adequacy and effectiveness of measures taken to address any deficiencies in those arrangements and procedures, including failures by the relevant persons to comply with such arrangements or follow such procedures.

- iv. take into consideration the internal capital adequacy assessment process in accordance with Sub-section 7, Section 3, Title 3 of this Chapter, if applicable.
- R3-3.1.3.1.2 The Licence Holder is required to establish and maintain a risk management function which independently carries out the following tasks:
 - i. the implementation of the policy and procedures referred to in R3-3.1.3.1.1; and
 - ii. the provision of reports and advice to senior management in accordance with R3-3.1.2.3.
- R3-3.1.3.1.3 The Licence Holder is required to establish and maintain a risk management function that operates independently and which has sufficient authority and resources, including access to the Board of Administration where necessary, to facilitate the carrying out of the following tasks:
 - i. the implementation of the policy and procedures referred to in this Title;
 - ii. the provision of reports and advice to senior management;
 - iii. the development of the Licence Holder's risk strategy and participation in all material risk management decisions; and
 - iv. direct communication with the Board of Administration in its supervisory function, independently from the Licence's Holder senior management, where appropriate, regarding concerns, where specific risk developments affect or may affect the Licence Holder, without prejudice to the responsibilities of the Board of Administration in its supervisory and/or managerial functions.
- R3-3.1.3.1.4 The MFSA may allow the Licence Holder to establish and maintain a risk management function which does not operate independently, provided this does not give rise to conflicts of interest and the Licence Holder demonstrates to the MFSA that the establishment and maintenance of a dedicated independent risk management function with sole responsibility for the risk management function is not appropriate and proportionate in view of the nature, scale and complexity of its business and the nature and range of the VFA services undertaken in the course of that business.
- R3-3.1.3.1.5 Where a Licence Holder is granted such derogation it must nevertheless be able to demonstrate that the policies and procedures which it has adopted in accordance with R3-3.1.3.1.1 satisfy the requirements thereof and are consistently effective.

Sub-Section 4 Compliance

R3-3.1.4.1 General Requirements

R3-3.1.4.1.1 The Licence Holder shall establish, implement and maintain adequate policies and procedures designed to detect any risk of failure by the Licence Holder to comply with its obligations under the Act, the VFA Regulations issued thereunder and these Rules, as well as with its obligations under other applicable legislation, as well as to detect the associated risks, and shall put in place adequate measures and procedures designed to minimize such risk and to enable the MFSA to exercise its powers effectively.

The Licence Holder shall, for this purpose, take into account the nature, scale and complexity of its business and the nature and range of VFA services undertaken in the course of that business

R3-3.1.4.1.2 The Licence Holder shall establish and maintain a permanent and effective compliance function which operates independently, and which has the following responsibilities:

- i. to monitor and, on a regular basis, to assess the adequacy and effectiveness of the measures and procedures put in place in accordance with the requirements of R3-3.1.4.1.1, and the actions taken to address any deficiencies in the Licence Holder's compliance with its obligations;
- ii. to draw up and implement a compliance monitoring plan; and
- iii. to advise and assist the relevant persons responsible for carrying out VFA services to comply with the Licence Holder's legal and regulatory obligations.

R3-3.1.4.1.3 In order to enable the compliance function to discharge its responsibilities properly, the Licence Holder shall ensure that the following conditions are satisfied:

- i. the compliance function shall have the necessary authority, resources, expertise and access to all relevant information;
- ii. a Compliance Officer shall be appointed and shall be responsible for the compliance function and for any reporting as to compliance required by these Rules;
- iii. the relevant persons involved in the compliance function shall not be involved in the performance of services or activities which they monitor; and

- iv. the method of determining the remuneration of the relevant persons involved in the compliance function shall not compromise their objectivity and shall not be likely to do so.
- R3-3.1.4.1.4 However, the MFSA may exempt a Licence Holder from the requirements of point (iii) of Rule R3-3.1.4.1.3 if the Licence Holder is able to demonstrate to the satisfaction of the MFSA, that in view of the nature, scale and complexity of its business, and the nature and range of VFA Services and related activities, the requirement under that point is not proportionate and that its compliance function continues to be independent, objective and effective.
- R3-3.1.4.1.5 Moreover, with respect to point (ii) of Rule R3-3.1.4.1.3, the appointment of an individual as Compliance Officer is subject to MFSA's prior approval. Such person may also act as the Licence Holder's Money Laundering Reporting Officer.
- R3-3.1.4.2 *Compliance Certificate*
- R3-3.1.4.2.1 The Licence Holder shall submit to the MFSA on an annual basis, together with the annual audited financial statements, a Compliance Certificate, drawn up by its Compliance Officer, which shall include:
 - i. the outcome of the Compliance Officer's Compliance Monitoring Plan, including a list of breaches identified thereof;
 - ii. a confirmation that all the local AML/CFT requirements have been satisfied, which confirmation should be obtained from the Licence Holder's MLRO; and
 - iii. a list of clients against whom disciplinary action has been taken by the Licence Holder, including a brief description of the client's breach, and the actions taken by the Licence Holder.
- R3-3.1.4.2.3 The Licence Holder shall ensure that the Compliance Certificate is signed by the Compliance Officer and countersigned by at least one Administrator.
- R3-3.1.4.2.4 A copy of the Compliance Certificate prepared in terms of R3-3.1.4.2 should be held at the registered address of the Licence Holder in Malta and made available to the MFSA and the FIAU upon request.
- R3-3.1.4.3 *The Financial Instrument Test*
- R3-3.1.4.3.1 In so far as a determination has not already been made by an Issuer pursuant to Chapter 2 of these Rules, a Licence Holder shall, in determining whether a DLT asset qualifies as a virtual financial asset and prior to offering a VFA service in relation to such DLT asset, undertake the Financial Instrument Test, which shall

be signed by the person responsible for carrying out the test, and counter-signed by at least one Administrator.

Provided that the MFSA shall not ordinarily make any determinations of its own with reference to a DLT asset's nature but shall rely on the determinations made by the Licence Holder; it should therefore be understood that in case of doubt the Licence Holder should obtain an external legal opinion.

R3-3.1.4.4 *Money Laundering Reporting Officer*

R3-3.1.4.4.1 The Licence Holder shall appoint and have at all times in place an MLRO. The role of the MLRO is an onerous one and the Licence Holder shall ensure that it is only accepted by individuals who fully understand the extent of responsibilities attached to the role.

R3-3.1.4.4.2 When appointing an MLRO, the Licence Holder shall ensure compliance with the applicable provisions of Part I of the Implementing Procedures as well as any sector-specific Implementing Procedures issued by the FIAU in terms of the provisions of the Prevention of Money Laundering and Funding of Terrorism Regulations.

R3-3.1.4.4.3 The Licence Holder shall ensure that the role of MLRO is only accepted by individuals who fully understand the extent of responsibilities attached to the role.

Sub-Section 5 ***Safeguarding of Clients' Assets***

R3-3.1.5.1 *General Requirements*

R3-3.1.5.1.1 Where the Licence Holder is authorised to hold or control clients' assets, it shall comply with the Rules in this Section in addition to the relevant provisions of the VFA Regulations.

R3-3.1.5.1.2 For purposes of safeguarding client's rights in relation to virtual financial assets and money belonging to them which are held or controlled by the Licence Holder, a Licence Holder shall hold clients' money and/or virtual financial assets in specially created and segregated accounts. These accounts must be identified separately from any accounts used to hold money and/or virtual financial assets belonging to the Licence Holder.

R3-3.1.5.1.3 The Licence Holder shall obtain a written declaration from the entities with whom the Licence Holder has deposited clients' assets in accordance with the VFA Regulations that that entity renounces and will not attempt to enforce or execute, any charge, right of set-off or other claim against the account, or combine the account with any other account in respect of any debt owed to

the it by the Licence Holder, and that interest payable on the account will be credited to the account.

R3-3.1.5.2 *Reconciliation of Clients' Money*

R3-3.1.5.2.1 The Licence Holder shall reconcile, at least on a monthly basis, the balance on each client's money account as recorded by the Licence Holder with the balance on that account as set out in the statement issued by the entity with whom the Licence Holder has deposited clients' money in accordance with the VFA Regulations.

R3-3.1.5.2.2 The Licence holder shall also reconcile the total of the balances on all clients' money accounts as recorded by the Licence Holder with the total of the corresponding credit balances in respect of each of its clients as recorded by the Licence Holder.

R3-3.1.5.3 *Reconciliation of Clients' Assets*

R3-3.1.5.3.1 The Licence Holder shall carry out reconciliations of clients' assets with customers' records at least on a monthly basis.

R3-3.1.5.3.2 Where the Licence Holder discovers discrepancies after carrying out the above reconciliations, it shall maintain a record of such discrepancies and the measures taken to remedy such differences.

R3-3.1.5.4 *Custody*

R3-3.1.5.4.1 A Licence Holder may appoint a Custodian for the safekeeping of its Assets and any virtual financial assets held for the account of its clients. The Licence Holder shall carry out a detailed assessment of the proposed Custodian, including *inter alia* the experience, systems and controls employed by the proposed Custodian.

R3-3.1.5.4.2 The Licence Holder shall notify the MFSA prior to the appointment or replacement of a Custodian pursuant to this Rule.

Provided that the MFSA may object to the proposed appointment or replacement and to require such additional information as it may consider appropriate.

R3-3.1.5.4.3 Where the business model of the Licence Holder involves the custody of Assets and investors' Funds, either by the Licence Holder itself or by a third-party Custodian, the said Licence Holder shall ensure that such service is provided in

line with internationally and nationally recognised best practices and cyber security standards, as well as any guidelines issued by the Authority.

Sub-Section 6 Other Organisational Requirements

R3-3.1.6.1 Internal Audit

R3-3.1.6.1.1 The Licence Holder shall establish and maintain an internal audit function which is separate and independent from the other functions and activities of the Licence Holder and which has the following responsibilities:

- i. to establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the Licence Holder's systems, internal control mechanisms and arrangements;
- ii. to issue recommendations based on the result of work carried out in accordance with point (i) of this Rule;
- iii. to verify compliance with those recommendations; and
- iv. to report in relation to internal audit matters.

R3-3.1.6.1.2 Provided that where appropriate and proportionate, in view of the nature, scale and complexity of its business and the nature and range of VFA services undertaken in the course of its business, the MFSA may, at its discretion, exempt the Licence Holder from the requirements set out by R3-3.1.6.1.1.

R3-3.1.6.2 Insurance Requirement

R3-3.1.6.2.1 Licence Holders shall make every effort to take out and maintain an insurance policy that covers loss of money or loss or damage to any other asset or property belonging to the Licence Holder or which is in the care, custody or control of the Licence Holder or for which the Licence Holder is responsible.

R3-3.1.6.2.2 The Licence Holder shall make every effort to take out and maintain full Professional Indemnity Insurance cover.

Provided that the Licence Holder shall notify the Authority whether it has managed to obtain a Professional Indemnity Insurance following its efforts pursuant to this Rule.

R3-3.1.6.2.3 The Licence Holder shall ensure that the Professional Indemnity Insurance cover is in line with market standards and adequately covers the risks associated with the business of the Licence Holder.

R3-3.1.6.2.4 For the purposes of demonstrating to the satisfaction of the MFSA that the requirements in this Section are being complied with on an on-going basis, the Licence Holder shall, upon request by the MFSA, submit to the MFSA a copy of the renewal cover note or such other written evidence as the MFSA may require to establish compliance with these Rules.

R3-3.1.6.2.5 A Licence Holder shall within two working days from the date it becomes aware of any of the circumstances specified in (i) to (vii) below, inform the MFSA in writing where:

- i. during the period of a policy, the Licence Holder has notified insurers of an incident which may give rise to a claim under the policy;
- ii. during the period of a policy, the insurer has cancelled the policy or has notified its intention of doing so;
- iii. the policy has not been renewed or has been cancelled and another policy satisfying the requirements of this Section has not been taken out from the day on which the previous policy lapsed or was cancelled;
- iv. during the period of a policy, the terms or conditions are altered in any manner so that the policy no longer satisfies the requirements of this Section; and
- v. the insurer has intimated that it intends to decline to indemnify the insured in respect of a claim under the policy.

R3-3.1.6.2.6 The required minimum limits of indemnity are:

- i. In respect of any one claim, the higher of:
 - a. three times Relevant Income; or
 - b. EUR 1,000,000 for Class 1 Licence Holders.

Plus legal costs limited to 20% of (a) or (b) of point (i) of this Rule, whichever is applicable.

- ii. In aggregate, the higher of:
 - a. three times Relevant Income; or
 - b. EUR 1,500,000 for Class 1 Licence Holders.

Plus legal costs limited to 20% of (a) or (b) of point (ii) of this Rule, whichever is applicable.

R3-3.1.6.3	<i>Business Continuity Process</i>
R3-3.1.6.3.1	<p>The business continuity process shall consist of:</p> <ol style="list-style-type: none"> i. a Disaster Recovery Plan ('DRP'); ii. a Business Continuity Plan ('BCP'); and iii. Business Continuity Management ('BCM').
R3-3.1.6.3.2	The DRP shall define the resources (hardware, software, communications, data as well as human resources), actions and tasks required for the recovery of the infrastructure needed to support the Licence Holder's business functions. This document may form part of the BCP.
R3-3.1.6.3.3	The BCP is a management process to ensure the continuity of businesses and shall define the advance planning and preparations that are necessary to minimise loss and ensure continuity of the critical business functions of a Licence Holder in the event of disruption. In this regard, the Licence Holder shall ensure that the BCP is available as a formal manual which is made available for reference to all the Licence Holder's personnel.
R3-3.1.6.3.4	BCM is an integral part of corporate governance and shall encompass the BCP and DRP and the Licence Holder shall integrate them into an ongoing strategic management process which identifies potential threats which may affect the Licence Holder. As part of BCM, the Licence holder shall also design a responsive framework to safeguard its interests as well as those of its customers.
R3-3.1.6.3.5	For purposes of this Rule, the Licence Holder shall ensure that the DRP, BCP and BCM comply with any applicable Guidelines issued by the Authority.
R3-3.1.6.4	<i>Outsourcing Requirements</i>
R3-3.1.6.4.1	<u>General</u>
R3-3.1.6.4.1.1	A Licence Holder shall ensure, when relying on a third party for the performance of any operational function, that it takes reasonable steps to avoid undue additional operational risk for the provision of continuous and satisfactory service to clients and the performance of VFA services on a continuous and satisfactory basis.
R3-3.1.6.4.1.2	When the Licence Holder outsources any operational functions or any VFA Services, the Licence Holder shall remain fully responsible for discharging all of their obligations under these Rules and shall adequately manage the risks relating to such outsourcing arrangements at all times.

- R3-3.1.6.4.1.3 The Licence Holder shall carry out an ongoing assessment of the operational risks and the concentration risk associated with all its outsourcing arrangements. The Licence Holder shall notify the MFSA of any material developments.
- R3-3.1.6.4.1.4 The ultimate responsibility for the proper management of the risks associated with outsourcing or the outsourced activities lies with the Licence Holder.
- R3-3.1.6.4.1.5 When the Licence Holder outsources any operational function or any VFA Services, the Licence Holder shall ensure that the outsourcing arrangements do not result in the delegation of its senior management's responsibility.
- R3-3.1.6.4.1.6 The outsourcing of operational functions may not be undertaken in such a way as to materially impair:
- i. the ability of the MFSA to monitor the Licence Holder's compliance with all obligations;
 - ii. the orderliness of the conduct of the outsourcing Licence Holder's business or of the VFA services provided;
 - iii. the quality of the Licence Holder's internal control;
 - iv. the senior management's ability to manage and monitor the Licence Holder's business and its licensed activities; and
 - v. the ability of other internal governance bodies, such as the Board of Administration or the audit committee, to fulfil their oversight tasks in relation to the senior management.
- R3-3.1.6.4.1.7 A Licence Holder shall inform the MFSA of any material outsourcing arrangements and shall make available on request all information necessary to enable the Authority to supervise the compliance of the performance of the outsourced activities with the requirements of these Rules.
- R3-3.1.6.4.1.8 A Licence Holder shall inform the MFSA of any material development affecting an outsourced activity and the manner by which it is proposing to rectify its position in order to fulfil its obligation to its customers.
- R3-3.1.6.4.1.9 Licence Holders shall not outsource management functions such as the setting of strategies and policies in respect of the Licence Holder's risk profile and control, the oversight of the operation of the Licence Holder's processes, and the final responsibility towards customers.
- R3-3.1.6.4.1.10 A Licence Holder shall not outsource services and activities concerning licensable activities unless the outsourcing service provider either:

- i. holds an equivalent authorisation as the Licence Holder outsourcing the services; or
- ii. is otherwise allowed to carry out those activities in accordance with the relevant national legal framework.

R3-3.1.6.4.1.11 The MFSA may impose specific conditions on the Licence Holder for the outsourcing of any activities.

R3-3.1.6.4.2 The Outsourcing Policy

R3-3.1.6.4.2.1 A Licence Holder shall have a policy on its approach to outsourcing, including contingency plans, exit strategies as well as a general policy that covers all aspects of outsourcing, including non-material outsourcing, whether the outsourcing takes place within a corporate group or not.

R3-3.1.6.4.3 The Outsourcing Contract

R3-3.1.6.4.3.1 The Licence Holder shall ensure that any outsourcing arrangement is based on a formal, clear, written contract which establishes the respective rights and obligations of the Licence Holder and of the service provider.

R3-3.1.6.5 *White Label Agreements*

R3-3.1.6.5.1 A Licence Holder shall inform the MFSA of any White Label Agreement it has entered into, and shall make available on request all information necessary to enable the Authority to supervise the compliance of the performance of its activities with the requirements of these Rules.

R3-3.1.6.5.2 Notwithstanding any White Label Agreement, the Licence Holder shall remain fully responsible for discharging all of its obligations under these Rules.

R3-3.1.6.6 Systems Audit Report

R3-3.1.6.6.1 Where a Licence Holder was required to appoint a Systems Auditor at application stage, in terms of Sub-Section 4, Section 1 of Title 2 of this Rulebook, the said Sub-Section, as well as Sub-Section 6, Section 1 of Title 2 of this Rulebook shall apply *mutatis mutandis* and any reference to an 'Applicant' therein shall be construed as a reference to a Licence Holder accordingly.

R3-3.1.6.7 *IT Audit Report*

R3-3.1.6.7.1 Where a Licence Holder was required to appoint an IT Auditor at application stage, in terms of Sub-Section 5, Section 1 of Title 2 of this Rulebook, the said Sub-Section, as well as Sub-Section 6, Section 1 of Title 2 of this Rulebook shall apply *mutatis mutandis* and any reference to an 'Applicant' therein shall be construed as reference to a Licence Holder accordingly.

R3-3.1.6.7.2 The Licence Holder shall ensure that its IT Auditor prepares an IT Audit Report in line with any internationally and nationally recognised standards, as well as any guidelines issued by the Authority, on an annual basis. Such report shall be required to be submitted to the MFSA together with the annual audited financial statements.

The IT Audit Report shall include a confirmation from the IT Auditor that the Licence Holder does not have an Innovative Technology Arrangement in place as part of its operations or operate a technological infrastructure which interacts with an Innovative Technology Arrangement in some way or form.

Provided that, subject to the nature, scale and complexity of the Licence Holder's business, the Authority may request that an IT Audit Report be submitted at more frequent intervals.

Sub-Section 7 *Procedures for Reporting of Breaches*

R3-3.1.7.1 The Licence holder shall develop and maintain appropriate procedures for employees to report breaches internally through a specific, independent and autonomous channel. Such a channel may also be provided through arrangements provided for by social partners and shall include at least:

- i. specific procedures for the receipt of reports on potential or actual infringements and their follow-up, including the establishment of secure communication channels for such reports;
- ii. appropriate protection for employees who report breaches committed within the Licence Holder against retaliation, discrimination or other types of unfair treatment;
- iii. protection of personal data concerning both the person who reports the breaches and the person who is allegedly responsible for a breach; and
- iv. clear rules ensuring that confidentiality is guaranteed in all cases in relation to the person who reports the breaches committed within the Licence Holder, unless disclosure is required by Maltese law in the context of further investigations or subsequent judicial proceedings.

R3-3.1.7.2 Licence Holders shall also refer to and comply with the applicable provisions of the Protection of the Whistleblower Act.

Section 2 Supplementary Conditions

Sub-Section 1 Scope and Application

R3-3.2.1.1 This Section sets out the Supplementary Conditions for particular types and, or Classes of Licence Holders.

R3-3.2.1.2 Sub-Section 2 sets out the Supplementary Conditions for VFA Exchanges and shall therefore solely apply to Class 4 Licence Holders.

Sub-Section 2 Supplementary Conditions applicable to VFA Exchanges

R3-3.2.2.1 Listing Criteria

R3-3.2.2.1.1 A Licence Holder shall, prior to admitting a virtual financial asset to trading on its platform, carry out appropriate research in order to assess the quality of the virtual financial asset.

R3-3.2.2.1.2 Pursuant to R3-3.2.2.1.1, when assessing the quality of a virtual financial asset, the Licence Holder shall take *inter alia* the following factors into account:

- i. The technological experience, track record and reputation of the issuer and its development team; and
- ii. the determination in accordance with the Financial Instrument Test in line with R3-3.1.4.3.

Provided that a Licence Holder shall not admit to trading on its platform any virtual financial asset which has an inbuilt anonymization function unless the holder and transaction history of the virtual financial asset can be identified.

R3-3.2.2.2 Suspension and removal from trading

R3-3.2.2.2.1 Without prejudice to the right of the Authority under the Act to demand suspension or removal of a virtual financial asset from trading, a Licence Holder may suspend or remove from trading a virtual financial asset which no longer complies with the rules of the VFA exchange unless such suspension or removal would be likely to cause significant damage to the investors' interests or the orderly functioning of the market.

R3-3.2.2.2.2 A Licence Holder that suspends or removes from trading a virtual financial asset shall make public its decision on the suspension or removal of the virtual financial asset.

Furthermore, where such decision carries regulatory implications, such decision shall be communicated to the MFSA.

R3-3.2.2.2.3 Where a Licence Holder has suspended or removed a virtual financial asset from trading, the Authority may require that other Licence Holders, which fall under its jurisdiction and trade the same virtual financial asset, also suspend or remove that virtual financial asset from trading.

R3-3.2.2.2.4 The competent authority shall immediately make public any decision taken pursuant to R3-3.2.2.2.

R3-3.2.2.3 *Order Matching*

R3-3.2.2.3.1 A Licence Holder shall ensure expedient and accurate verification of trades and matching settlement instructions.

R3-3.2.2.3.2 A Licence Holder shall ensure that it is capable of verifying the existence of Funds and Assets, as applicable, of persons submitting orders.

R3-3.2.2.4 *Pre-trade and Post-trade transparency*

R3-3.2.2.4.1 Pre-trade Transparency

R3-3.2.2.4.1.1 Licence Holders shall make public current bid and offer prices and the depth of trading interests at those prices which are advertised through their systems for virtual financial assets traded on their platform.

Provided that the Authority may, at its discretion, and on a case by case basis, waive the obligation for Licence Holders to make such information public.

R3-3.2.2.4.1.2 Pursuant to R3-3.2.2.4.1.1, Licence Holders shall make the information available to the public on a continuous basis during trading hours.

R3-3.2.2.4.2 Post-trade Transparency

R3-3.2.2.4.2.1 Licence Holders shall make public the price, volume and time of the transactions executed in respect of virtual financial assets traded on their platforms. Licence Holders shall make details of all such transactions public as close to real-time as is technically possible.

R3-3.2.2.4.3 Obligation to make pre-trade and post-trade data available

- R3-3.2.2.4.3.1 Licence Holders shall make the information published in accordance with R3-3.2.2.4.1 and R3-3.2.2.4.2 available to the public by offering pre-trade and post-trade transparency data separately.
- R3-3.2.2.4.3.2 Licence Holders shall make the information published in accordance with R3-3.2.2.4.1 and R3-3.2.2.4.2 available to the public on a reasonable commercial basis and ensure non-discriminatory access to the information. Such information shall be made available free of charge 15 minutes after publication.
- R3-3.2.2.5 *Client Record Keeping*
- R3-3.2.2.5.1 Licence Holders shall keep at the disposal of the Authority, for at least five years, the relevant data relating to all orders and all transactions in virtual financial assets which are carried out through their systems.
- R3-3.2.2.5.2 Pursuant to R3-3.2.2.5.1, the records shall contain the relevant data that constitute the characteristics of the order, including those that link an order with the executed transaction(s) that stems from that order. This shall include:
- i. details of the names and numbers of the virtual financial assets bought or sold;
 - ii. the quantity;
 - iii. the dates and times of execution;
 - iv. the transaction prices; and
 - v. a designation to identify the clients in relation to which that transaction has been executed.
- R3-3.2.2.5.3 Licence Holders shall maintain adequate resources and have back-up facilities in place in order to be capable of reporting at all times.
- R3-3.2.2.6 *Reporting of Suspicious Transactions*
- R3-3.2.2.6.1 A Licence Holder shall immediately report to the Authority any transaction which breaches or which the Licence Holder suspects to have breached, the Act, particularly Part VI thereof, the VFA Regulations issued thereunder, and these Rules.
- R3-3.2.2.7 *System Resilience*

- R3-3.2.2.7.1 A Licence Holder shall have in place effective systems, procedures and arrangements to ensure its trading systems are resilient, have sufficient capacity to deal with peak order and message volumes, are able to ensure orderly trading under conditions of severe market stress, are fully tested to ensure such conditions are met and are subject to effective business continuity arrangements to ensure continuity of its services if there is any failure of its trading systems
- R3-3.2.2.7.2 A Licence Holder shall have in place effective systems, procedures and arrangements to reject orders that exceed pre-determined volume and price thresholds or are clearly erroneous.
- R3-3.2.2.7.3 A Licence Holder shall be able to temporarily halt or constrain trading if there is a significant price movement in a virtual financial asset on its platform or a related platform during a short period and, in exceptional cases, to be able to cancel, vary or correct any transaction.
- R3-3.2.2.7.4 A Licence Holder shall ensure that its rules on co-location services are transparent, fair and non-discriminatory.
- R3-3.2.2.7.5 A Licence Holder shall ensure that its fee structures are transparent, fair and non-discriminatory and that they do not create incentives to place, modify or cancel orders or to execute transactions in a way which contributes to disorderly trading conditions or market abuse.
- R3-3.2.2.7.6 A Licence Holder may adjust its fees for cancelled orders according to the length of time for which the order was maintained and to calibrate the fees to each virtual financial asset to which they apply.
- R3-3.2.2.7.7 Licence Holders shall, upon request by the Authority, make available to the Authority, data relating to the order book or give the Authority access to the order book so that it is able to monitor trading.
- R3-3.2.2.8 *Settlement*
- R3-3.2.2.8.1 Licence Holders shall establish procedures that enable the confirmation of relevant details of transactions in virtual financial assets.
- Provided that Licence Holders shall take measures to limit the number of settlement fails.
- R3-3.2.2.8.2 The Licence Holder's procedures should clearly define the point at which settlement is final.
- R3-3.2.2.8.3 A Licence Holder shall complete final settlement no later than the end of the value date, and preferably intraday or in real time, to reduce settlement risk.

- R3-3.2.2.8.4 A Licence Holder shall clearly define the point after which unsettled payments, transfer instructions, or other obligations may not be revoked by a client.
- R3-3.2.2.8.5 A Licence Holder shall minimise and strictly control the credit and liquidity risk arising from money settlements.
- R3-3.2.2.8.6 A Licence Holder shall clearly state its obligations with respect to the delivery of virtual financial assets and should identify, monitor, and manage the risks associated with such delivery.
- R3-3.2.2.8.7 A Licence Holder shall have in place adequate systems to safeguard against settlement failures and resolution systems which cater for such failures. Such systems should be clearly documented in the Licence Holder's bye-laws.
- R3-3.2.2.8.8 A Licence Holder shall establish a system that monitors settlement fails of transactions in virtual financial assets. It shall provide regular reports to the Authority, as to the number and details of settlement fails and any other relevant information. Those reports shall be made public by the Licence Holder in an aggregated and anonymised form on an annual basis.
- R3-3.2.2.9 *Bye-Laws*
- R3-3.2.2.9.1 A Licence Holder shall issue clear and transparent bye-laws in order to ensure that any virtual financial asset being traded on its platform is being traded in a fair, orderly and efficient manner. Such bye-laws, and any changes or amendments thereto are to be approved by the Licence Holder's Board of Administration.
- Provided that the bye-laws shall be reviewed by the VFA Agent at application stage, and by the Compliance Officer on an ongoing basis thereafter.
- Provided further that the Authority may require a Licence Holder to effect any changes to its bye-laws, as it may deem necessary.
- R3-3.2.2.10 *Inability to Discharge Functions*
- R3-3.2.2.10.1 Where, due to the occurrence of any event or circumstances, a Licence Holder is unable to discharge any of its functions whatsoever, it must give the Authority notice of its inability to discharge that function without undue delay, specifying:
- i. the event or circumstance causing it to become unable to discharge any of its functions;
 - ii. the functions which the Licence Holder is unable to discharge; and

- iii. what action, if any, is being taken or is being proposed by the Licence Holder in order to deal with the situation and, in particular, to be able to recommence discharging that function.

R3-3.2.2.11 *Synchronisation of Business Clocks*

R3-3.2.2.11.1 Licence Holders shall synchronise the business clocks they use to record the date and time of any reportable event.

Section 3 Prudential Requirements

Sub-Section 1 Scope and Application

R3-3.3.1.1 This Section shall apply to all Licence Holders falling within scope of these Rules, except for:

- i. R3-3.3.4.2, which shall apply solely to Class 2, Class 3 and Class 4 Licence Holders;
- ii. Sub-Section 7 of this Section, which shall apply solely to Class 2, Class 3 and Class 4 Licence Holders; and
- iii. Sub-Section 8 of this Section, which shall apply solely to Class 2, Class 3 and Class 4 Licence Holders.

R3-3.3.1.2 A Licence Holder shall comply with the requirements laid down in this Section on an individual basis.

R3-3.3.1.3 This Section sets out the uniform prudential requirements applicable to VFA Service Providers, which *inter alia*, include (i) the initial capital requirement, (ii) the capital requirement and (iii) the liquidity requirement.

R3-3.3.1.4 The Authority may review this Section, or any parts thereof, as it may deem necessary.

Sub-Section 2 Own Funds Requirements

R3-3.3.2.1 A Licence Holder shall have own funds consisting of the sum of its Tier 1 capital and Tier 2 capital where:

- i. at least 56 % of the sum shall consist of Common Equity Tier 1 Capital;
- ii. up to 44 % of the sum may consist of Additional Tier 1 Capital; and

- iii. up to 25% of the sum may consist of Tier 2 Capital.

Provided that for the purposes of the determination of own funds, the following shall not apply:

- i. the threshold exemptions referred to in Article 48 of Regulation (EU) No 575/2013;
- ii. the deductions referred to in Articles 46, 60 and 70 of Regulation (EU) No 575/2013;
- iii. the trigger event referred to in Article 54(1)(a) of Regulation (EU) No 575/2013. The trigger event shall instead be specified by the Licence Holder in the terms of the additional Tier 1 instrument as specified in R3-3.3.2.1; and
- iv. the aggregate amount referred to in Article 54(4)(a) of Regulation (EU) No 575/2013. The amount to be written down or converted shall be the full principal amount of the additional Tier 1 instrument as specified in R3-3.3.2.1.

R3-3.3.2.2 Pursuant to R3-3.3.2.1, a Licence Holder shall apply the provisions set out in Chapter 6 of Title 1 in Part Two of Regulation (EU) No 575/2013 where determining the own funds requirements.

Sub-Section 3 Initial Capital Requirement

R3-3.3.3.1 The initial capital applicable to each respective class of VFA Service Providers required at the time of authorisation pursuant to R3-2.2.3.4.2 is indicated in Table R3-2.

R3-3.3.3.2 The initial capital of a Licence Holder shall consist of one or more of the items referred to in Sub-section 2 of this Section.

R3-3.3.3.3 The initial capital of Licence Holders may also be complemented with a Professional Indemnity Insurance cover as set out in R3-3.1.6.2.2, as applicable.

TABLE R3-2: INITIAL CAPITAL REQUIREMENTS FOR VFA SERVICE PROVIDERS

VFA Services Licence	Initial Capital Requirement (EUR)		
Class 1	i.	50,000	OR
	ii.	25,000 and PII	
Class 2		125,000	
Class 3		730,000	
Class 4		730,000	

Sub-Section 4 Capital Requirement

- R3-3.3.4.1 The Licence Holders shall at all times maintain, at a minimum, own funds equal to their capital requirement, which shall amount to the higher of the following:
- i. its permanent minimum requirement calculated according to Sub-section 5 of this Section; or
 - ii. its fixed overheads requirement calculated according to Sub-section 6 of this Section.
- R3-3.3.4.2 The Licence Holder shall also hold additional capital to that referred to in R3-3.3.4.1, on the basis of the internal capital adequacy assessment process as set out in Sub-section 7 of this Section.
- R3-3.3.4.3 The Licence Holder may also be required by the Authority to hold additional capital to that referred to in R3-3.3.4.1.
- R3-3.3.4.4 The Licence Holder shall immediately notify the MFSA if at any time it is in breach of its capital requirement. In this case, the MFSA may, if the circumstances justify it, allow the Licence Holder a limited period within which to restore its capital requirement to the required level.

Sub-Section 5 Permanent minimum requirement

- R3-3.3.5.1 For the purposes of point (i) of R3-3.3.4.1, the permanent minimum requirement shall amount to at least the levels of initial capital specified in Sub-section 3 of this Section.

Sub-Section 6 Fixed Overhead Requirement

- R3-3.3.6.1 For the purposes of point (ii) of R3-3.3.4.1, the fixed overheads requirement shall amount to at least one quarter of the fixed overheads of the preceding year.
- R3-3.3.6.2 For the purposes of R3-3.3.6.1, the Licence Holder shall calculate its fixed overheads of the preceding year, using figures resulting from the applicable accounting framework, by subtracting the following items from the total expenses after distribution of profits to Unitholders in their most recent audited annual financial statements, or, where audited statements are not available, in annual financial statements validated by the Authority:
- i. fully discretionary staff bonuses;

- ii. employees', directors' and partners' shares in profits, to the extent that they are fully discretionary;
- iii. other appropriation of profits and other variable remuneration, to the extent that they are fully discretionary;
- iv. shared commissions and fees payable which are directly related to commission and fees receivable, which are included within total revenue, and where the payment of the commission and fees payable is contingent upon the actual receipt of the commission and fees receivable;
- v. fees, brokerage and other charges paid to clearing houses, exchanges and intermediate brokers for the purposes of executing, registered or clearing transactions;
- vi. interest paid to customers on clients' money; and
- vii. non-recurring expenses from non-ordinary activities.

R3-3.3.6.3 Where fixed expenses have been incurred on behalf of the Licence Holder by third parties, and these fixed expenses are not already included within the total expenses referred to in R3-3.3.6.2, the Licence Holder shall take either of the following actions:

- i. where a break-down of the expenses of those third parties is available, Licence Holders shall determine the amount of fixed expenses that those third parties have incurred on their behalf and shall add that amount to the figure resulting from R3-3.3.6.2; or
- ii. where the break-down referred to in point (i) is not available, the Licence Holders shall determine the amount of expenses incurred on their behalf by those third parties according to the Licence Holder's business plans and shall add that amount to the figure resulting from R3-3.3.6.2.

R3-3.3.6.4 Where the Licence Holder's most recent audited financial statements do not reflect a twelve-month period, it shall divide the result of the calculation of R3-3.3.6.2 by the number of months that are reflected in those financial statements and shall subsequently multiply the result by twelve, so as to produce an equivalent annual amount.

R3-3.3.6.5 Where the Licence Holder has not completed business for one year from the day it commences its business, it shall use the projected fixed overheads included in its budget for the first twelve months' of business, as submitted with its application for authorisation and as approved by the Authority, for the year following the year of commencement of its business.

- R3-3.3.6.6 Where there is a change in the business of a Licence Holder since the preceding year that the Authority considers to be material, the Authority may adjust the requirement laid down in R3-3.3.6.1.

Sub-Section 7 Internal Capital Adequacy Assessment Process

- R3-3.3.7.1 The Licence Holder shall have in place sound, effective and comprehensive strategies and processes to assess and maintain on an ongoing basis the amounts, types and distribution of internal capital that they consider adequate to cover the nature and level of risks to which it is or might be exposed.
- R3-3.3.7.2 The strategies and processes referred to in R3-3.3.7.1 shall be subject to regular internal review to ensure that they remain comprehensive and proportionate to the nature, scale and complexity of the activities of the Licence Holder.

Sub-Section 8 Liquidity Requirement

- R3-3.3.8.1 The Licence Holder shall at all times hold as a minimum, an amount of liquid assets equivalent to at least one third of the fixed overhead requirements calculated in accordance with Sub-Section 6 of this Section for their liquidity requirement.
- R3-3.3.8.2 The Licence Holder should have an internal liquidity management policy and procedures which assess, monitor and manage its liquidity requirement. The policy and procedures should ensure that the Licence Holder has a resilient liquidity risk profile, which allows it to continue operating normally under liquidity stressed scenarios.
- R3-3.3.8.3 Pursuant to R3-3.3.8.2, the Licence Holder shall also include as part of the liquidity management policy, the methodology by which assets are assessed to be considered as liquid assets for the purposes of this Sub-section. When assessing whether an asset may qualify as a liquid asset the Licence Holder shall consider unencumbered assets, that consist of:
- i. cash; and
 - ii. assets that can be converted into cash at little or no loss of value.
- R3-3.3.8.4 For the purposes of point (ii) of R3-3.3.8.3, the following characteristics should be taken consideration:
- i. fundamental characteristics:
 - a. low risk;

- b. easily obtainable, accurate and reliable valuation;
 - c. low correlation with other assets or assets classes; and
 - d. high transparency.
- ii. market-related characteristics:
 - a. active and sizable market;
 - b. low volatility; and
 - c. flight to quality.

R3-3.3.8.5 Further to R3-3.3.8.3, a Licence Holder may also include receivables from trade debtors and fees or commissions receivable within 30 days in their liquid assets, where those receivables comply with the following conditions:

- i. they account for up to one third of the minimum liquidity requirements as referred to in R3-3.3.8.1;
- ii. they are not to be counted towards any additional liquidity requirements required by the competent authority for firm-specific risk; and
- iii. they are subject to a haircut of 50%.

R3-3.3.8.6 A Licence Holder may, in exceptional circumstances, reduce the amount of liquid assets held. Where such reduction occurs, the Licence Holder shall immediately notify the Authority without delay.

R3-3.3.8.7 Compliance with the liquidity requirement set out in R3-3.3.8.1 shall be restored within 30 days of the original reduction.

Section 4 Conduct of Business Obligations

Sub-Section 1 General Scope and Application

R3-3.4.1.1 This Section sets out the Conduct of Business Obligations which Licence Holders must adhere to.

R3-3.4.1.2 This Section shall apply to all VFA Service Providers except for:

- i. Sub-Section 4 which shall apply solely to VFA Service Providers executing clients' orders; and

- ii. R3-3.4.4.1.2 which shall not apply to persons operating a VFA Exchange.

Sub-Section 2 Conflicts of Interest

R3-3.4.2.1 General Obligations

R3-3.4.2.1.1 Licence Holders shall adopt appropriate and transparent reporting lines within its organisation in order to ensure that issues involving risks of non-compliance with conflicts of interest rules are given the necessary priority.

R3-3.4.2.1.2 A Licence Holder shall establish, implement and maintain effective organisational and administrative arrangements appropriate to the size and organisation of the Licence Holder and the nature, scale and complexity of its business, to prevent conflicts of interest from adversely affecting the interests of its Clients.

R3-3.4.2.1.3 The circumstances which should be treated as giving rise to a conflict of interest should cover cases where there is a conflict between the interests of the Licence Holder or certain persons connected to the Licence Holder or the group of which the Licence Holder forms part, or from the performance of services and activities, and the duty the Licence Holder owes to a Client; or between the differing interests of two or more of its Clients, to whom the Licence Holder owes in each case a duty.

R3-3.4.2.1.4 A Licence Holder shall establish, implement and maintain an effective conflicts of interest policy set out in writing and which is appropriate to the size and organisation of the Licence Holder and the nature, scale and complexity of its business, to prevent conflicts of interest from adversely affecting the interests of its Clients.

R3-3.4.2.1.5 A Licence Holder shall keep and regularly update a record of the situations or service carried out by or on behalf of the Licence Holder in which a conflict of interest entailing a risk of damage to the interests of one or more Clients has arisen or, in the case of an ongoing VFA service, may arise. Senior Management shall receive on a frequent basis, and at least annually, written reports on situations referred to in this Rule.

R3-3.4.2.2 Operational Independence Rules

R3-3.4.2.2.1 A Licence Holder shall take all appropriate steps to identify and to prevent or manage conflicts of interest between themselves, including their managers, employees, or any person directly or indirectly linked to them by control and their Clients or between the interests of one Client and another, including those caused by the receipt of inducements from third parties or by a Licence Holder's own remuneration and other incentive structures.

- R3-3.4.2.2.2 The Board of Administration of a Licence Holder shall define, oversee and be accountable for the implementation of governance arrangements that ensure effective and prudent management of the Licence Holder including the segregation of duties within that Licence Holder and the prevention of conflicts of interest, and in a manner that promotes the integrity of the market and the interest of Clients.
- R3-3.4.2.3 *Conflict of Interest Policy Rules*
- R3-3.4.2.3.1 The conflict of interest policy established in accordance with these Rules shall be set out in writing and shall include the following:
- i. The identification of, with reference to the specific distribution activities, specific services, activities and ancillary services carried out by or on behalf of the Licence Holder, the circumstances which constitute or may give rise to a conflict of interest entailing a risk of damage to the interests of one or more Clients; and
 - ii. Procedures to be followed and measures to be adopted in order to manage such conflicts and to prevent such conflicts from damaging the interests of Clients.
- R3-3.4.2.3.2 The Licence Holder shall assess and periodically review, at least annually, the conflict of interest policy established in accordance with these Rules and shall take all appropriate measures to address any deficiencies.
- R3-3.4.2.4 *Remuneration Policy Rules*
- R3-3.4.2.4.1 A Licence Holder shall define and implement remuneration policies and practices under appropriate internal procedures taking into account the interests of all its Clients. The remuneration policy should be periodically reviewed.
- R3-3.4.2.4.2 In defining its remuneration policies, a Licence Holder shall ensure that:
- i. Clients are treated fairly and their interests are not impaired by the remuneration practices adopted by the Licence Holder in the short, medium or long term; and
 - ii. Remuneration policies and practices do not create a conflict of interest or incentive that may lead Relevant Persons to favour their own interests or the Licence Holder's interest to the potential detriment of its Clients.

- R3-3.4.2.4.3 The Licence Holder's Board of Administration shall approve the remuneration policy, after taking advice from the compliance function. Senior management of the Licence Holder shall be responsible for the day-to-day implementation of the remuneration policy and the monitoring of compliance risks related to the said policy.
- R3-3.4.2.4.4 A Licence Holder's remuneration policies and practices shall include and provide for the maintenance of measures enabling the Licence Holder to effectively identify where the Licence Holder fails to act in the best interests of a Client and to take remedial action without undue delay.
- R3-3.4.2.5 *Inducements Rules*
- R3-3.4.2.5.1 A Licence Holder shall not accept and retain fees, commissions or any monetary or non-monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of VFA Services to Clients. All such fees, commissions or monetary benefits received from third parties in relation to the provision of VFA Services shall be transferred in full to the Client.
- Provided that minor non-monetary benefits that are capable of enhancing the quality of service provided to a Client and are of a scale and nature such that they could not be deemed to impair compliance with the Licence Holder's duty to act in the best interest of the Client shall be clearly disclosed and would be excluded from the application of this Rule.
- R3-3.4.2.5.2 A Licence Holder shall set up and implement a policy to ensure that any fees, commissions or any monetary or non-monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of VFA Services are allocated and transferred to each individual Client.
- R3-3.4.2.5.3 A Licence Holder shall inform Clients about the fees, commissions or any monetary or non-monetary benefits transferred to them, such as through the periodic reporting statements provided to the Client.
- R3-3.4.2.5.4 The Board of Administration shall adopt and at least annually review the general principles of the inducements policy, and shall be responsible for and oversee its implementation. The Board of Administration shall also ensure that the Compliance Officer is involved in the establishment and the subsequent reviews of the inducements policy.
- R3-3.4.2.5.5 A Licence Holder shall not receive any remuneration, discount or non-monetary benefit for routing Client orders to a particular trading venue or execution venue which would infringe the requirements on conflicts of interest or inducements.

R3-3.4.2.6 *Personal Transaction Rules*

R3-3.4.2.6.1 A Licence Holder shall establish, implement and maintain adequate arrangements which prevent any Relevant Person who is involved in activities that may give rise to a conflict of interest, or who has access to inside information or to other confidential information relating to Clients or transactions with or for Clients by virtue of an activity carried out by him on behalf of the Licence Holder.

R3-3.4.2.6.2 Licence Holders shall ensure that Relevant Persons do not enter into a personal transaction which meets at least one of the following criteria:

- i. that the person is prohibited from entering into it in terms of the Part VI of the Act;
- ii. it involves the misuse or improper disclosure of confidential information; or
- iii. it conflicts or is likely to conflict with an obligation of the Licence Holder under the Act, the VFA Regulations or the Rules issued thereunder, as applicable.

Sub-Section 3 Sale Processes and Selling Practices

R3-3.4.3.1 *General Principles*

R3-3.4.3.1.1 A Licence Holder shall *inter alia*:

- i. seek from its Clients information relevant to the virtual financial asset or VFA Service requested;
- ii. in the completion of any document, make it clear that all the answers or statements regarding the Client's personal details and circumstances are the Client's own responsibility. The Client should always be required to assume responsibility for the completed document and be advised that incomplete and/or inaccurate information may prejudice the Client's rights;
- iii. not withhold from the Client any written evidence or documentation relating to the virtual financial asset or VFA Service without adequate and justifiable reasons being disclosed in writing and without delay to the Client;
- iv. not recklessly, negligently or deliberately mislead a Client in relation to the real or perceived advantages or disadvantages of any virtual financial asset or VFA Service;

- v. ensure that all instructions from or on behalf of a Client are processed properly and promptly;
- vi. have proper regard for the wishes of a Client who seeks to terminate any agreement with it to carry out business;
- vii. seek to avoid conflicts of interest;
- viii. not exert undue pressure or undue influence on a Client;
- ix. give Advice only on those virtual financial assets or VFA Services in which the Licence Holder is knowledgeable and seek or recommend other specialist Advice when necessary;
- x. treat all information supplied by the Client with complete confidentiality; and
- xi. not request Clients to sign declarations to the effect that s/he has understood and accepts certain features of the virtual financial asset or that s/he is relying on his/her own skill, judgement and expertise when it is the obligation of the Licence Holder to assess the suitability of such virtual financial asset vis-à-vis the Client.

R3-3.4.3.1.2 Any information acquired by a Licence Holder from a Client shall not be used or disclosed except in the normal course of negotiating, maintaining or renewing a virtual financial asset or VFA Service for that Client or in accordance with the provisions of specific legislation or unless the consent of the Client has been obtained.

R3-3.4.3.1.3 The Licence Holder shall acknowledge receipt to the Client of all money received in connection with a virtual financial asset or VFA Service and that any charge or fee imposed shall be disclosed separately.

Provided that the term 'money' shall be deemed for the purposes of this Rule to include virtual financial assets which function as means of payment:

Provided further that the requirements above may be satisfied by means of documentation in electronic form.

R3-3.4.3.1.4 A Licence Holder shall not:

- i. make inaccurate or unfair criticism of any other Licence Holder or any virtual financial asset offered by such other Licence Holder;

- ii. make comparisons with other types of virtual financial assets or VFA Services unless the differing characteristics of each virtual financial asset or VFA Service are made clear;
- iii. persuade or attempt to persuade a Client to surrender or cancel any virtual financial asset or VFA Service which such Client may have already purchased, if such surrender or cancellation is not in the best interest of the Client; or
- iv. in general, entice Clients to purchase virtual financial assets or VFA Services it offers by giving or promising to give gifts to such Clients. Any gifts which the Licence Holder may offer its Clients must be related to the virtual financial asset or VFA Service being offered and/or enhance the value thereof. Such gifts should not be of a substantial value.

R3-3.4.3.2 *Contact with Clients*

R3-3.4.3.2.1 The Licence Holder shall ensure that staff who deal with Clients:

- i. are civil and considerate;
- ii. do not use undue pressure, deception or artificiality;
- iii. make plain their purpose;
- iv. do not harass or cajole Clients or force them to purchase a virtual financial asset or VFA Service;
- v. avoid contacts during unsocial hours, observe the Conduct of Business Rules in this section and ensure that no deals are finalised on the sole basis of a telephone conversation unless previously agreed otherwise in writing with the Client; and
- vi. Do not continue with the dialogue if requested by the Client to desist.

R3-3.4.3.3 *Client Categorisation*

R3-3.4.3.3.1 A Licence Holder shall, before providing a Service within the meaning of the Act, classify a Client to whom the Service is to be offered as an Experienced Investor or Non-Experienced Investor.

R3-3.4.3.3.2 The Licence Holder shall:

- i. notify a new Client of its categorisation as a Non-Experienced Investor; and

- ii. Prior to the provision of a VFA Service, inform a Client in a durable medium about:
 - a. any right which that Client has to request a different categorisation; and
 - b. any limitations to the level of Client protection that such a different categorisation would entail.

R3-3.4.3.3.3 Experienced Investors

R3-3.4.3.3.3.1 An Experienced Investor may be either a *per se* Experienced Investor or an Elective Experienced Investor.

R3-3.4.3.3.3.2 The Licence Holder shall inform Experienced Investors of their categorisation and that they are responsible for keeping the Licence Holder informed about any change, which could affect their current categorisation.

Provided that the Licence Holder shall take appropriate action in the event that it becomes aware that the Client no longer fulfils the initial conditions, which made him/her eligible for professional treatment.

R3-3.4.3.3.3.3 The Licence Holder shall deem a person which falls under the definition of Experienced Investor in terms of the Glossary to these Rules as a *Per Se Experienced Investor*.

R3-3.4.3.3.3.4 A Licence Holder may treat a Client as an *Elective Experienced Investor* if it complies with points (i), (ii) and (iii) below:

- i. The Licence Holder undertakes an adequate assessment of the expertise, experience and knowledge of the Client, and this assessment gives reasonable assurance, in light of the nature of the transactions or Services envisaged, that the Client is capable of making his own investment decisions and of understanding the risks involved ("the qualitative test").
- ii. In the course of the assessment referred to in point (i) above, as a minimum, two of the following criteria shall be satisfied:
 - a. the Client has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter of the previous four quarters;
 - b. the size of the Client's virtual financial asset portfolio, defined as including cash deposits and virtual financial assets exceeds, EUR 500 000 or its currency equivalent;

- c. the Client works or has worked in a position, which requires knowledge of the transactions or Services envisaged;
 - d. the Client has worked in the financial sector for at least one year in a professional position ("the quantitative test").
- iii. The following procedure is followed:
- a. they shall state in writing to the Licence Holder that they wish to be treated as an Experienced Investor, either generally or in respect of a particular VFA Service or transaction or type of transaction or virtual financial asset;
 - b. the Licence Holder shall give such Clients a clear written warning of the protections and investor compensation rights they may lose; and
 - c. Clients shall state in writing in a separate document from the contract, that they are aware of the consequences of losing such protections.

Provided that where the Client is not a natural person, the qualitative test should be performed in relation to the person authorised to carry out transactions on its behalf.

R3-3.4.3.3.3.5 Before deciding to accept any request for re-categorisation as an Elective Experienced Investor, a Licence Holder must take all reasonable steps to ensure that the Client requesting to be treated as an Elective Experienced Investor satisfies the qualitative test and the quantitative test referred to above.

R3-3.4.3.3.3.6 If a Licence Holder becomes aware that a Client no longer fulfils the initial conditions that made it eligible for categorisation as an Elective Experienced Investor, the Licence Holder must take the appropriate action. Where such appropriate action involves re-categorising that Client as a Non-Experienced Investor, the Licence Holder must notify that Client of its new categorisation.

R3-3.4.3.3.4 Non-Experienced Investors

R3-3.4.3.3.4.1 The Licence Holder shall treat as a Non-Experienced Investor any Client which does not satisfy the requirements of the classification as an Experienced Investor, or any Client who has requested to be treated as a Non-Experienced Investor.

R3-3.4.3.3.5 Higher Level of Protection

R3-3.4.3.3.5.1 If a *Per Se Experienced Investor* requests treatment as a Non-Experienced Investor, the Client will be classified as a Non-Experienced Investor if it enters into a

written agreement with the Licence Holder to the effect that it will not be treated as an Experienced Investor for the purposes of the applicable conduct of business regime.

R3-3.4.3.3.6 Policies and Procedures to Categorise Clients

R3-3.4.3.3.6.1 The Licence Holder shall implement appropriate written internal policies and procedures to categorise Clients.

R3-3.4.3.4 *Advice and non-Advice*

R3-3.4.3.4.1 A Licence Holder shall be deemed to provide Advice for the purposes of these Rules if it provides a Personal Recommendation to a client, either at the request of the Client in question or on its own initiative, with respect to virtual financial assets.

R3-3.4.3.4.2 Where a Licence Holder informs the Client that Advice is provided on an independent basis, that Licence Holder shall conduct a fair and comprehensive analysis of the market by assessing a sufficient range of virtual financial assets available on the market which shall be sufficiently diverse to ensure that the Client's needs and objectives can be suitably met.

R3-3.4.3.4.3 A Licence Holder informing a Client that Advice is provided on an independent basis shall define and implement a selection process to assess and compare a sufficient range of virtual financial assets available on the market.

Provided that where such a comparison is not possible because of the business model or the specific scope of the Service provided, the Licence Holder providing Advice should not be allowed to claim itself as "independent".

R3-3.4.3.4.4 Non-Independent Advice is any advice which does not qualify as Independent Advice within the meaning of R3-3.4.3.4.

R3-3.4.3.4.5 A Licence Holder shall explain in a clear and concise way whether and why Advice qualifies as independent or non-independent and the type and nature of the restrictions that apply, including, when providing Advice on an independent basis, the prohibition to receive and retain inducements.

R3-3.4.3.4.6 Where Advice is offered or provided to the same Client on both an independent and non-independent basis, Licence Holders shall explain the scope of both services to allow clients to understand the differences between them and not present itself as an independent advisor for the overall activity. Licence Holders shall not give undue prominence to their independent Advice services over non-independent Advice services in their communications with Clients.

R3-3.4.3.5 *Assessment of Clients' Suitability*

R3-3.4.3.5.1 Licence Holders shall ensure and demonstrate to the Authority, that natural persons giving Advice or information about virtual financial assets or VFA Services to Clients on behalf of the Licence Holder possess the necessary knowledge and competence to fulfil their obligations under these Rules.

R3-3.4.3.5.2 The Licence Holder's responsibility to perform the suitability assessment as delineated in this Section shall not be reduced due to the fact that Advice on virtual financial assets is provided in whole or in part through an automated or semi-automated system.

R3-3.4.3.6 *Suitability*

R3-3.4.3.6.1 A Licence Holder shall understand the virtual financial asset/s it offers or recommends, assess the compatibility of such virtual financial assets with the needs of the Clients to whom it provides VFA Services and ensure that such virtual financial assets are offered or recommended only when this is in the interest of the Client.

R3-3.4.3.6.2 Licence Holders shall implement policies and procedures to enable them to collect and assess all information necessary to conduct a suitability assessment for each Client.

R3-3.4.3.6.3 Licence Holders shall not create any ambiguity or confusion about their responsibilities in the process when assessing the suitability of virtual financial assets or VFA Services. When undertaking the suitability assessment, the Licence Holder shall inform Clients or potential Clients, clearly and simply, that the reason for assessing suitability is to enable the Licence Holder to act in the Client's best interest.

R3-3.4.3.6.4 Assessment of Suitability

R3-3.4.3.6.4.1 Information on Advice and Portfolio Management services should include information about the suitability assessment. 'Suitability assessment' should be understood as meaning the whole process of collecting information about a Client, and the subsequent assessment of the suitability of a given virtual financial asset for that Client.

R3-3.4.3.6.4.2 When providing Advice or Portfolio management services to a Client, the Licence Holder must first obtain the necessary information regarding the Client's:

- i. knowledge and experience in the investment field relative to the specific type of the virtual financial asset or VFA Service;

- ii. financial situation including his ability to bear losses; and
- iii. investment objectives including risk tolerance

so as to enable the Licence Holder to recommend to the Client, virtual financial assets which are suitable for him and, in particular, are in accordance with his risk tolerance and ability to bear losses.

R3-3.4.3.6.4.3 Licence Holders shall take reasonable steps to ensure that the information collected about their Clients is reliable.

R3-3.4.3.6.4.4 Licence Holders shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of VFA Services and virtual financial assets selected for their Clients and that they assess, while taking into account cost and complexity, whether equivalent VFA Services or virtual financial assets could meet their Client's profile.

R3-3.4.3.6.4.5 When providing Advice or Portfolio Management services that involve switching investments, either by selling a virtual financial asset and buying another, or by exercising a right to make a change in regard to an existing virtual financial asset, a Licence Holder shall collect the necessary information on the Client's existing investments and the recommended new virtual financial assets to undertake an analysis of the costs and benefits of the switch, such that the Licence Holder is reasonably able to demonstrate that the benefits of switching are greater than the costs.

R3-3.4.3.6.4.6 Where the Licence Holder has an ongoing relationship with the Client, the Licence Holder shall have, and be able to demonstrate, appropriate procedures to maintain adequate and up-to-date information about the Client.

R3-3.4.3.6.4.7 When providing the Services of Advice or Portfolio Management, a Licence Holder shall not recommend or decide to trade where none of the VFA Services or virtual financial assets are suitable for the Client.

R3-3.4.3.6.5 Suitability Statement

R3-3.4.3.6.5.1 A Licence Holder, when providing Advice or Portfolio Management Services to a Client shall, before providing the said Service, furnish the Client with a suitability statement.

Provided that when providing Portfolio Management Services, the Licence Holder shall provide a suitability statement to the Client on a quarterly basis.

R3-3.4.3.6.6 Contents of Suitability Statement

R3-3.4.3.6.6.1 The suitability statement shall, as a minimum:

- i. specify the Client's financial demands and needs;
- ii. provide an outline of the Advice given, where applicable; and
- iii. explain why the Licence Holder has concluded that the recommended transaction is suitable for the Client, including how it meets the Client's objectives and personal circumstances with reference to the investment term required, Client's knowledge and experience and client's attitude to risk and capacity for loss.

R3-3.4.3.6.6.2 The Licence Holder shall establish appropriate safeguards in order to ensure that the Client does not incur a loss as a result of an inaccurate or unfair presentation of the Personal Recommendation in the report presenting such Personal Recommendation. Such unfair or inaccurate presentation may relate, *inter alia*, to the manner in which the Personal Recommendation is indicated as suitable for the Client or to the disadvantages of the recommended course of action.

R3-3.4.3.6.6.3 Where a Licence Holder provides a Service that involves periodic suitability assessments and reports, the subsequent reports after the initial Service is established may only cover changes in the Services or virtual financial assets involved and/or the circumstances of the Client and may not need to repeat all the details of the first report.

R3-3.4.3.6.6.4 A Licence Holder providing a periodic assessment of the suitability of the recommendations provided pursuant to R3-3.4.3.6.5 shall disclose all of the following:

- i. the frequency and extent of the periodic suitability assessment and, where relevant, the conditions that trigger that assessment;
- ii. the extent to which the information previously collected will be subject to reassessment; and
- iii. the way in which an updated recommendation will be communicated to the Client.

R3-3.4.3.6.6.5 Licence Holders providing a periodic suitability assessment shall review, in order to enhance the Service, the suitability of the recommendations given at least annually.

The frequency of this assessment shall be increased depending on the risk profile of the Client and the type of virtual financial asset recommended.

R3-3.4.3.7 *Risk Disclosure*

R3-3.4.3.7.1 When providing a VFA Service other than Advice or Portfolio Management, a Licence Holder shall appropriately warn clients of the risks associated with investing in virtual financial assets through a Risk Disclosure Document.

R3-3.4.3.8 *Further Provisions to the Assessment of Suitability*

R3-3.4.3.8.1 Licence Holders shall ensure that the information regarding the Client's knowledge and experience with regards to virtual financial assets includes the following, to the extent appropriate to the nature of the Client, the nature and extent of the VFA Service to be provided and to the type of virtual financial asset or transaction envisaged, including their complexity and risks involved:

- i. the type of virtual financial asset/s or VFA Service/s with which the Client is familiar;
- ii. the nature, volume, frequency of the Client's transactions in the relevant virtual financial asset/s and the period over which they have been carried out; and
- iii. the level of education, profession or relevant former profession of the Client.

R3-3.4.3.8.2 A Licence Holder shall be entitled to rely on the information provided by its Clients unless it is aware or ought to be aware that the information is manifestly out-of-date, inaccurate or incomplete.

R3-3.4.3.9 *Suitability Assessment Tools/Questionnaires*

R3-3.4.3.9.1 A Licence Holder assessing a Client's knowledge and experience with respect to a virtual financial asset, shall ensure that:

- i. the Client understands the particular features of the virtual financial asset. This should entail clear answers from specific questions presented to the Client about the features of the virtual financial assets in order to confirm that the Client is effectively aware of the features and risks of the virtual financial asset in question;
- ii. the documentation used for the testing of knowledge and experience should clearly indicate the VFA Service being provided to the Client and in the context of which the test is being carried out; and
- iii. In the case of Non-Experienced Investors, Licence Holders shall provide the documentation used to assess the suitability of a virtual financial

asset also in the language agreed between the Client and the Licence Holder.

R3-3.4.3.10 *Contractual Arrangements with Clients*

R3-3.4.3.10.1 A Licence Holder shall ensure that the terms of any contract or agreement entered into with a Client for the provision of a VFA Service, are fair, clear and not misleading.

R3-3.4.3.10.2 A Licence Holder shall establish a record that includes the document or documents agreed between the Licence Holder and the Client that set out the essential rights and obligations of the parties, and the other terms on which the Licence Holder will provide VFA Services to the Client. The rights and duties of the parties to the contract may be incorporated by reference to other documents or legal texts.

R3-3.4.3.10.3 The Licence Holder shall not, in any communication or agreement with a Client (except where permitted by applicable legislation), exclude or restrict, or seek to exclude or restrict:

- i. any legal liability or duty of care to a Client which it has under applicable law or under these Rules;
- ii. any other duty to act with skill, care and diligence which is owed to a Client in connection with the provision to that Client of a virtual financial asset or VFA Service; or
- iii. any liability owed to a Client for failure to exercise the degree of skill, care and diligence that may reasonably be expected of it in the provision of a virtual financial asset or VFA Service.

R3-3.4.3.10.4 Licence Holders providing any VFA Service shall enter into a written basic agreement with the Client, in paper or another durable medium, setting out the essential rights and obligations of the Licence Holder and the Client. Licence Holders providing Advice shall comply with this obligation only where a periodic assessment of the suitability of the virtual financial assets or VFA Services recommended is performed.

R3-3.4.3.10.5 Pursuant to R3-3.4.3.10.4 above, the written agreement shall set out the essential rights and obligations of the parties, and shall *inter alia* include the following:

- i. a description of the VFA Services, and where relevant the nature and extent of any Advice services to be provided;

- ii. in case of Portfolio Management services, the types of virtual financial assets that may be purchased and sold and the types of transactions that may be undertaken on behalf of the Client, as well as any virtual financial assets or transactions prohibited; and
- iii. a description of the main features of any of the VFA Services to be provided relating to safekeeping and administration of virtual financial assets for the account of clients.

R3-3.4.3.11 *Complaints Handling by Licence Holders*

R3-3.4.3.11.1 Complaints Management Policy

R3-3.4.3.11.1.1 Licence Holders shall ensure that a complaints management policy is put in place and set out in a written document. This policy shall be defined and endorsed by the Licence Holder's senior management, who shall also be responsible for its implementation and for monitoring compliance with it.

R3-3.4.3.11.1.2 A Licence Holder shall make the complaints management policy available to all its relevant staff through an adequate internal channel.

R3-3.4.3.11.2 Complaints Management Function

R3-3.4.3.11.2.1 Licence Holders shall have in place a complaints management function which enables them to investigate complaints fairly and to identify or mitigate any possible conflicts of interest.

R3-3.4.3.11.2.2 Licence Holders shall inform the Authority of the identity and contact details of the individual/s involved in the complaints management function as referred to above and any changes thereto.

R3-3.4.3.11.3 Registration of Complaints

R3-3.4.3.11.3.1 Licence Holders shall register any complaints it receives in an appropriate manner, as soon as these are received together with any action taken with respect to such complaints. The Authority may at any time require the register to be produced for its review.

R3-3.4.3.11.4 Internal Follow-up of Complaints

R3-3.4.3.11.4.1 Licence Holders shall analyse, on an on-going basis, complaints handling data to ensure that they identify and address any recurring or systemic problems and potential legal and operational risks.

R3-3.4.3.11.5 Provision of Information

R3-3.4.3.11.5.1

Licence Holders shall:

- i. on request or when acknowledging receipt of a complaint, provide written information regarding their complaints handling process;
- ii. publish details of their complaints handling process in an easily accessible manner;
- iii. provide clear, accurate and up-to-date information about the complaints-handling process including:
 - a. details of how to make a complaint; and
 - b. the process that will be followed when handling a complaint.
- iv. keep the complainant informed about further handling of the complaint.

R3-3.4.3.11.6

Procedure for Responding to Complaints

R3-3.4.3.11.6.1

Licence Holders shall:

- i. in writing, acknowledge receipt of any complaint upon receipt;
- ii. where a complaint is made orally, the Licence Holder shall make a summary of the complaint and request the complainant to confirm in writing the said summary;
- iii. seek to gather and investigate all relevant evidence and information regarding the complaint;
- iv. communicate in plain language, which is clearly understood;
- v. provide a response without unnecessary delay, or at least, by not later than fifteen working days from when the complaint was registered. Where the investigation of a complaint is not completed within fifteen days from receipt of the complaint, the Licence Holder shall:
 - a. inform the complainant about the causes of the delay; and
 - b. provide an indication as to when the investigation is likely to be completed;
- vi. when providing a final decision in terms of point (v) above that does not fully satisfy the complainant's demand, shall provide a thorough explanation of the Licence Holder's position on the complaint and that if the complainant is not satisfied with the way the complaint was

resolved by the Licence Holder, the complainant may refer the complaint to the Office of the Arbiter for Financial Services established under the Arbiter for Financial Services Act, (Cap.555). Such decision shall be provided in writing.

R3-3.4.3.11.7 Reporting to the Authority

R3-3.4.3.11.7.1 Licence Holders shall provide information on complaints and complaints handling to the Authority as and when required in any format as required by the Authority. This data shall, as a minimum, cover the number of complaints received, differentiated as appropriate by virtual financial asset or VFA Service, as applicable, and the cause of the complaint.

R3-3.4.3.11.7.2 Without prejudice to R3-3.4.3.11.7.1 above, where a complaint has been lodged with the Office of the Arbiter for Financial Services and the case has been decided, the Licence Holder shall immediately provide the Authority with a copy of the Arbiter's final decision. The Licence Holder shall also notify the Authority immediately, in the event that an appeal from the decision of the Arbiter is lodged by the complainant or by the Licence Holder itself, in terms of the Arbiter for Financial Services Act, and once such appeal has been decided of the final decision of the Court.

R3-3.4.3.11.8 Arbiter for Financial Services

R3-3.4.3.11.8.1 The Licence Holder is required to establish, implement and maintain effective and transparent procedures for the reasonable and prompt handling of each complaint received from clients, and to keep a record of each complaint and the measures taken for its resolution. The Licence Holder is also required to inform eligible complainants in writing that they may refer their complaint to the Office of the Arbiter for Financial Services as established by the Arbiter for Financial Services Act, if they are not satisfied with the manner in which it has been handled by the Licence Holder.

Sub-Section 4 ***Execution of Clients' Orders***

R3-3.4.4.1 *Obligation to execute orders on terms most favourable to the Client*

R3-3.4.4.1.1 A Licence Holder shall take all sufficient steps to obtain, when executing orders, the best possible result for its Clients taking into account the best execution factors of price, costs, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order.

R3-3.4.4.1.2 When executing orders, the Licence Holder shall check the fairness of the price proposed to the Client, by gathering market data used in the estimation of the

price of such virtual financial asset and, where possible, by comparing with similar or comparable virtual financial assets.

R3-3.4.4.1.3 Whenever there is a specific instruction from the Client, the Licence Holder shall execute the order following the specific instruction. The Licence Holder shall be deemed to have satisfied its obligations under this Sub-Section to take all reasonable steps to obtain the best possible result for a Client to the extent that it executes an order or a specific aspect of the order following specific instructions from a Client relating to the order or the specific aspect of the order.

R3-3.4.4.1.4 A Licence Holder shall, prior to the provision of the VFA Service, provide a Non-Experienced Investor with a clear and prominent warning that any specific instructions from a Client may prevent the Licence Holder from taking the steps that it has designed and implemented in its execution policy to obtain the best possible result for the execution of those orders in respect of the elements covered by those instructions.

R3-3.4.4.1.5 Further to R3-3.4.4.1.1, where a Licence Holder executes an order on behalf of a Non-Experienced Investor, the following shall also be taken into consideration in order to determine the best possible result:

- i. the total consideration, representing the price of the virtual financial asset; and
- ii. the costs relating to execution, which shall include expenses incurred by the Client which are directly related to the execution of the order, including execution venue fees, clearing and settlement fees and any other fees paid to third parties involved in the execution of the order.

R3-3.4.4.2 *Order execution policy*

R3-3.4.4.2.1 A Licence Holder shall establish and implement effective execution arrangements to ensure compliance with this Sub-Section. In particular a Licence Holder shall establish and implement an order execution policy to allow it to obtain, for its Client orders, the best possible result.

R3-3.4.4.2.2 A Licence Holder shall ensure that the venue or entity it selects will enable it to obtain results for its Clients that are at least as good as the results that it reasonably could expect from using alternative entities.

R3-3.4.4.2.3 Licence Holders shall provide appropriate information to their Clients on their order execution policy. That information shall explain clearly, in sufficient detail and in a way that can easily be understood by Clients.

R3-3.4.4.2.4 The Licence Holder shall obtain the prior consent of their Clients to the order execution policy.

R3-3.4.4.3 *Monitoring and Review*

R3-3.4.4.3.1 A Licence Holder shall review, at least on an annual basis, its execution policy and order execution arrangements established in terms of this Sub-Section.

R3-3.4.4.3.2 A Licence Holder shall demonstrate to its Clients, at their request, that it has executed their orders in accordance with the Licence Holder's order execution policy and it shall also ensure that it is able to demonstrate to the MFSA upon request that the Licence Holder is in compliance with these Rules.

R3-3.4.4.4 *Client Order Handling Rules*

R3-3.4.4.4.1 When carrying out Client orders, a Licence Holder shall implement procedures and arrangements which provide for the prompt, fair and expeditious execution of Client orders, relative to other Client orders or the trading interests of the Licence Holder.

R3-3.4.4.4.2 A Licence Holder shall not misuse information relating to pending Client orders, and shall take all reasonable steps to prevent the misuse of such information by any of its Relevant Persons.

R3-3.4.4.4.3 A Licence Holder shall not carry out a Client order or a transaction for own account in aggregation with another Client order unless the following conditions are met:

- i. it must be unlikely that the aggregation of orders and transactions will work overall to the disadvantage of a Client whose order is to be aggregated;
- ii. it must be disclosed to each Client whose order is to be aggregated that the effect of aggregation may work to its disadvantage in relation to a particular order; and
- iii. an order allocation policy must be established and effectively implemented, provided for the fair allocation of aggregated orders and transactions, including how the volume and price of orders determines allocations and the treatment of partial executions.

R3-3.4.4.4.4 Where a Licence Holder has aggregated transactions for own account with one or more Clients' orders, such Licence Holder shall not allocate the related trades in a way that is detrimental to a Client.

R3-3.4.4.4.5 Where a Licence Holder aggregates a Client order, with a transaction for own account and the aggregated order is partially executed, the Licence Holder shall allocate the related trades to the Client in priority to itself.

Provided that if the Licence Holder is able to demonstrate on reasonable grounds that without the combination it would not have been able to carry out the order on such advantageous terms, or at all, it may allocate the transaction for own account proportionally, in accordance with its order allocation policy.

R3-3.4.4.4.6 The Licence Holder shall, as part of the order allocation policy, put in place procedures designed to prevent the reallocation, in a way that is detrimental to the Client, of transactions for own account which are executed in combination with Client orders.

R3-3.4.4.5 *Reporting Obligations*

R3-3.4.4.5.1 A Licence Holder shall notify Clients with whom it has an ongoing Client relationship of any material changes to its order execution arrangements or order execution policy.

R3-3.4.4.6 *Selection of Execution Venues by Licence Holders*

R3-3.4.4.6.1 A Licence Holder shall not receive any remuneration, discount or non-monetary benefit for routing Client orders to a particular trading venue or execution venue which would be in breach of the requirements on conflicts of interest or inducements set out in this Rulebook.

R3-3.4.4.6.2 A Licence Holder shall not structure or charge its commission in such a way as to discriminate unfairly between execution venues.

Sub-Section 5 Virtual Financial Assets in relation to which services may be conducted

R3-3.4.5.1 A Licence Holder shall not perform services in relation to any virtual financial asset which has an inbuilt anonymization function unless the holder and transaction history of that virtual financial asset can be identified.

Section 5 Record Keeping, Reporting and Disclosure Requirements

Sub-Section 1 Scope and Application

R3-3.5.1.1 This Section sets out the record keeping, reporting and disclosure requirements which must be followed by VFA Service Providers.

R3-3.5.1.2 This Section applies to all VFA Service Providers falling within scope of these Rules.

*Sub-Section 2 Record Keeping and Accounting Records**R3-3.5.2.1 Record Keeping*

R3-3.5.2.1.1 The Licence Holder shall arrange for Records to be kept of all services and transactions undertaken by it which shall be sufficient to enable MFSA to monitor compliance with the requirements under these Rules, and in particular to ascertain that the Licence Holder has complied with all obligations with respect to clients or potential clients.

Provided that the requirements set out in this Section shall be without prejudice to:

- i. any other record keeping obligations that the Issuer may have in terms of any other law, rules or regulation; and
- ii. the right of any other authority, in terms of applicable law, to access the documents, data or information covered by this Section.

R3-3.5.2.1.2 In this regard, Records shall include the recording of telephone conversations and electronic communications involving transactions when dealing on own account and the provision of client order services that relate to the reception, transmission and execution of client orders.

R3-3.5.2.1.3 Moreover, the Licence Holder shall keep at the disposal of the MFSA, for at least five years, the relevant data relating to all transactions in virtual financial assets which it has carried out, whether on own account or on behalf of a client. The Authority may request that such records are kept for a period of up to 7 years.

R3-3.5.2.1.4 The Records shall be retained in a medium that allows the storage of information in a way accessible for future reference by the MFSA and in such a form and manner that the following conditions are met:

- i. the MFSA must be able to access them readily in a legible format and to reconstitute each key stage of the processing of each transaction; and
- ii. it must not be possible for the records otherwise to be manipulated or altered.

R3-3.5.2.1.5 The Licence Holder shall ensure that its IT infrastructure ensures:

- i. the integrity and security of any data stored therein;
- ii. availability, traceability and accessibility of data; and
- iii. privacy and confidentiality.

- R3-3.5.2.1.6 The Licence Holder shall ensure that its IT infrastructure is located in Malta, and/or any other EEA member state and/or any other third country jurisdiction wherein the Authority is satisfied that the requirements of R3-3.5.2.1.5 can be satisfied.
- R3-3.5.2.2 *Customers' Accounting Records*
- R3-3.5.2.2.1 The Licence Holder shall ensure that proper accounting records are kept to show and explain transactions processed by the Licence Holder on behalf of its customers.
- R3-3.5.2.2.2 The records shall:
- i. record all purchases and sales of Customers' Assets processed by the Licence Holder;
 - ii. record all receipts and payments of money belonging to customers which arise from transactions processed by the Licence Holder;
 - iii. disclose the assets and liabilities of a Licence Holder's customers individually and collectively, to the extent that they are managed by the Licence Holder; and
 - iv. record all Customers' Assets in the possession of the Licence Holder or of another person who is holding such assets for, or to the order of the Licence Holder, showing the location of the assets, their beneficial owner and the extent to which they are subject to any charge of which the Licence Holder has been notified.
- R3-3.5.2.2.3 Customers' accounting records shall be retained for a minimum period of ten years.
- R3-3.5.2.2.4 During the first two years they shall be kept in a place from which they can be produced within 24 hours of their being requested.
- R3-3.5.2.3 *Accounting Records*
- R3-3.5.2.3.1 The Licence Holder shall have internal control mechanisms and administrative and accounting procedures which permit the verification of their compliance with these Rules as well as effective procedures for risk assessment and effective control and safeguard arrangements for information processing systems.
- R3-3.5.2.3.2 The Licence Holder shall maintain proper accounting records to show and explain the Licence Holder's own transactions, assets and liabilities.

- R3-3.5.2.3.3 The accounting records shall:
- i. disclose with reasonable accuracy, at all times, the financial position of the Licence Holder; and
 - ii. enable the financial statements required by the MFSA to be prepared within the applicable time limits.

- R3-3.5.2.3.4 In particular, the financial records shall contain:
- i. entries from day to day of all sums of money received and expended and the matters to which they relate;
 - ii. a record of all income and expenses, explaining their nature;
 - iii. a record of all assets and liabilities, including any guarantees, contingent liabilities or other financial commitments; and
 - iv. entries from day to day of all transactions on the Licence Holder's own account.

R3-3.5.2.3.5 The Licence Holder shall retain accounting records for a minimum period of ten years. During the first two years they shall be kept in a place from which they can be produced within 24 hours of their being requested.

R3-3.5.2.3.6 The Licence Holder shall agree with the MFSA its accounting reference date.

Sub-Section 3 Appointing an Auditor

R3-3.5.3.1 The Licence Holder shall appoint an Auditor approved by the MFSA. The Licence Holder shall replace its Auditor if requested to do so by the MFSA. The MFSA's consent shall be sought prior to the appointment or replacement of an Auditor.

R3-3.5.3.2 The Licence Holder shall make available to its Auditor the information and explanations he needs to discharge his responsibilities as an Auditor and in order to meet the MFSA's requirements.

- R3-3.5.3.3 The Licence Holder shall not appoint an individual as an Auditor, nor appoint an audit firm where the individual directly responsible for the audit, or his firm is:
- i. an Administrator, Qualifying Holder, officer, representative or employee of the Licence Holder;
 - ii. a partner of, or in the employment of, any person in (i) above;

- iii. a spouse, civil partner, parent, step-parent, child, step-child or other close relative of any person in (i) above;
- iv. a person who is not otherwise independent of the Licence Holder; or
- v. person disqualified by the MFSA from acting as an Auditor of a Licence Holder.

R3-3.5.3.4 For this purpose, an Auditor shall not be regarded as an officer or an employee of the Licence Holder solely by reason of being Auditor of that Licence Holder.

R3-3.5.3.5 The Licence Holder shall obtain from its Auditor a signed letter of engagement defining clearly the extent of the Auditor's responsibilities and the terms of his appointment. The Licence Holder shall confirm in writing to its Auditor its agreement to the terms in the letter of engagement. The Auditor shall provide the MFSA with a letter of confirmation.

R3-3.5.3.6 If at any time the Licence Holder fails to have an Auditor in office for a period exceeding four weeks, the MFSA shall be entitled to appoint a person to fill the vacancy; the fees and charges so incurred being payable by the Licence Holder.

Sub-Section 4 Reporting Requirements

R3-3.5.4.1 General

R3-3.5.4.1.1 The Licence Holder shall prepare the Audited Annual Financial Return, the Annual Financial Return and Interim Financial Returns as specified in R3-3.5.4.2 to R3-3.5.4.4.

R3-3.5.4.1.2 The Licence Holder shall prepare and submit such additional financial returns as the MFSA may require. The Licence Holder shall be responsible for the correct compilation of such returns.

R3-3.5.4.2 Audited Annual Reporting Requirements

R3-3.5.4.2.1 The Licence Holder shall be required to submit to the MFSA, within four months from the accounting reference date, the soft and hard copies of the following:

- i. the automated Annual Audited Financial Return;
- ii. an original copy of the audited annual financial statements prepared in accordance with generally accepted accounting principles and practice;
- iii. a copy of the Auditor's management letter;

- iv. an original copy of the Auditor's report; and
 - v. an original copy of the Auditor's confirmation to the MFSA as specified in R3-3.5.4.2.7.
- R3-3.5.4.2.2 Pursuant to point (i) of Rule R3-3.5.4.2.1, the Licence Holder should ensure that the Annual Audited Financial Return is signed by:
 - i. at least two Administrators; or
 - ii. any other persons authorised to sign by way of a Board Resolution, a certified true copy of which is expected to be provided by the Licence Holder to the MFSA; and
 - iii. the Auditor.
- R3-3.5.4.2.3 Pursuant to point (ii) of R3-3.5.4.2.1, the Licence Holder shall also require its Auditor to prepare a management letter in accordance with International Standards on Auditing.
- R3-3.5.4.2.4 Furthermore, pursuant to point (ii) of R3-3.5.4.2.1, the Licence Holder is required to include in the Administrators' Report or by way of a separate confirmation signed by the Administrators, as applicable under the generally accepted accounting principles and practices, a statement regarding breaches of the Rules or other regulatory requirements which occurred during the reporting period, and which were subject to an administrative penalty or other regulatory sanction.
- R3-3.5.4.2.5 The Administrators' Report or the confirmation signed by the Administrators, as applicable, shall contain a summary of the breach/breaches committed and regulatory sanction/s imposed, if any. Where there have been no breaches, it shall contain a statement to that effect.
- R3-3.5.4.2.6 Pursuant to point (iii) of R3-3.5.4.2.1, the Licence Holder in receipt of a management letter from its Auditor which contains recommendations to remedy any weaknesses identified during the course of the audit, is required to submit to the MFSA by not later than six months from the end of the financial period to which the management letter relates, a statement setting out in detail the manner in which the Auditor's recommendations have been/ are being implemented. In the instance where the Licence Holder has not taken / is not taking any action in respect of any one or more recommendations in the Auditor's management letter, the reasons are to be included.
- R3-3.5.4.2.7 Pursuant to point (iv) of R3-3.5.4.2.1, the Auditor must also confirm to the MFSA that the audit has been conducted in accordance with International Standards on Auditing and whether, in the Auditor's opinion:

- i. the Annual Financial Return together with the audited annual financial statements are in agreement with the Licence Holder's accounting records;
- ii. the Annual Financial Return has been prepared in accordance with the MFSA's requirements and is consistent with the audited annual financial statements;
- iii. the Licence Holder's Financial Resources have been properly calculated in accordance with the MFSA's requirements and exceed the Licence Holder's Financial Resources Requirement as at the accounting reference date;
- iv. proper accounting records have been kept, and adequate systems for their control have been maintained, as required by the MFSA, during the period covered by the Annual Financial Return;
- v. based on review procedures performed, nothing has come to the Auditor's attention that causes the Auditor to believe that the Licence Holder held Clients' Assets during the period covered by the Annual Financial Return; and
- vi. all information and explanations necessary for the purpose of the audit have been obtained.

R3-3.5.4.2.8 Where, in the Auditor's opinion, one or more of the requirements have not been met, the Auditor shall be required to include in his report a statement specifying the relevant requirements and the respects in which they have not been met. Where the Auditor is unable to form an opinion as to whether the requirements have been met, the Auditor shall be required to specify the relevant requirements and the reasons why he has been unable to form an opinion.

R3-3.5.4.3 *Annual Financial Return*

R3-3.5.4.3.1 The Licence Holder shall each year prepare and submit the soft copy of the automated Annual Financial Return to the MFSA within one month from the accounting reference date.

R3-3.5.4.3.2 The Licence Holder shall also submit the original Representations Sheet of the Annual Financial Return.

R3-3.5.4.3.3 The Licence Holder should ensure that the Annual Financial Return is signed by:

- i. at least two Administrators; or

- ii. any other persons authorised to sign by way of a Board Resolution, a certified true copy of which is expected to be provided by the Licence Holder to the MFSA.

R3-3.5.4.3.4 Where the Annual Financial Return has been submitted before the relevant audited annual financial statements have been produced, it shall be updated to reflect the information in the audited financial statements and submitted to the MFSA together with the audited annual financial statements.

R3-3.5.4.4 *Interim Financial Returns*

R3-3.5.4.4.1 The Licence Holder shall prepare an automated Interim Financial Return ("IFR"), at dates three, six and nine months after the accounting reference date. The first IFR should cover the three months immediately following the accounting reference date, the second IFR should cover the six months immediately following the accounting reference date and the third IFR should cover the nine months immediately following the accounting reference date. In the event of a change to the accounting reference date, the dates for the preparation of the IFRs shall be agreed with the MFSA.

R3-3.5.4.4.2 The soft copy of the automated IFR shall be submitted to the MFSA within one month from the date up to which it has been prepared.

R3-3.5.4.4.3 The Licence Holder shall also submit the original Representations Sheet of the Interim Financial Return.

R3-3.5.4.4.4 The Licence Holder should ensure that the Interim Financial Return is signed by:

- i. by at least two Administrators; or
- ii. any other persons authorised to sign by way of a Board Resolution, a certified true copy of which is expected to be provided by the Licence Holder to the MFSA.

R3-3.5.4.5 *Risk Management and the Internal Capital Adequacy Assessment Report*

The Licence Holder shall prepare a Risk Management and the Internal Capital Adequacy Assessment Report, which shall be submitted to the Authority on an annual basis with the submission of the Audited Annual Reporting Requirements.

R3-3.5.4.5.1 The report shall outline the Licence Holder's compliance with the requirements laid down in:

- i. Sub-section 3, Section 1, Title 3 of this Chapter on Risk Management, which shall include (i) risk identification; (ii) description of risk; (iii) risk estimation; (iv) risk tolerance and evaluation; (v) risk treatment; and (vi) risk recording.
- ii. Sub-Section 7, Section 3, Title 3 of this Chapter on the Internal Capital Adequacy Assessment Process and the additional capital requirement which may be required in accordance with R3-3.3.4.2.

R3-3.5.4.5.2 The Licence Holder shall, on an annual basis, review its report with the aim of ensuring that this process remains comprehensive and proportionate to the nature, scale and complexity of the activities of the Licence Holder concerned.

Provided that for the purposes of point (ii) of this Rule, the Licence Holder shall indicate the figures within the report on a quarterly basis.

R3-3.5.4.5.3 The Licence Holder should ensure that the Risk Management and the Internal Capital Adequacy Assessment Report is signed by:

- i. by at least two Administrators; or
- ii. any other persons authorised to sign by way of a Board Resolution, a certified true copy of which is expected to be provided by the Licence Holder to the MFSA.

Title 4 Enforcement and Sanctions

Section 1 Scope and Application

R3-4.1.1 This Title provides detail with regards to administrative penalties and sanctions. It *inter alia* provides the principles which guide the MFSA when imposing an administrative penalty and provides for aggravating and mitigating circumstances in case of misconduct by VFA Service Providers.

Section 2 Enforcement and Sanctions

R3-4.2.1 The VFA Service Providers shall at all times observe the Rules which are applicable to it, as well as all the relative requirements which emanate from the Act and the VFA Regulations issued thereunder. In terms of the Act, the MFSA has various sanctioning powers which may be used against a Licence Holder which does not comply with its regulatory obligations. Such powers include the right to impose administrative penalties.

R3-4.2.2 Where a VFA Service Provider breaches or infringes a Rule, the MFSA may, by virtue of the authority granted to it under Article 48 of the Act, impose administrative penalties, without recourse to a court of law, up to a maximum of EUR 150,000.

R3-4.2.3 In determining whether to impose a penalty or other sanction, and in determining the appropriate penalty or sanction, the MFSA shall be guided by the principle of proportionality. The MFSA shall, where relevant, take into consideration the circumstances of the specific case, which may *inter alia* include:

- i. the repetition, frequency, gravity or duration of the infringement by the Licence Holder;
- ii. the degree of responsibility of the person responsible for the infringement;
- iii. the financial strength of the Licence Holder;
- iv. the profits gained or losses avoided by the Licence Holder by reason of the infringement, insofar as they can be determined;
- v. the losses for third parties caused by the infringement, insofar as they can be determined;
- vi. the level of cooperation of the Licence Holder with the Authority;

- vii. previous infringements by the Licence Holder and prior sanctions imposed by the MFSA or other regulatory authorities on the same Licence Holder;
- viii. the good faith, the degree of openness and diligence of the Licence Holder in the fulfilment of his obligations under the Act, VFA Regulations, Rules and Licence Conditions or of decisions of the competent authority in this regard;
- ix. any evidence of wilful deceit on the part of the Licence Holder or its officers; and
- x. any potential systemic consequences of the infringement.

- R3-4.2.4 Whenever the infringement consists of a failure to perform a duty, the application of a sanction shall not exempt the Licence Holder from its performance, unless the decision of the MFSA explicitly states the contrary.
- R3-4.2.5 These Rules stipulate various requirements for the submission of Documents within set time-frames. In the instance when such time-frames are not complied with, and unless there are justifiable reasons for the delay, Licence Holders will be considered as breaching the relevant Rule/s and will be penalised accordingly.
- R3-4.2.6 Documents may be submitted in various ways. The date of receipt will be as follows:
- i. if it is sent by fax or email, the date of receipt recorded shall be the time stamp of the fax or email, respectively;
 - ii. if it is sent by post, this will be the date indicated by the MFSA stamp evidencing receipt;
 - iii. if it is delivered by hand, on the date such delivery was made and recorded by the MFSA.
- R3-4.2.7 The MFSA will use its discretion to decide what action to take in respect of Licence Holders who do not submit Documents by their due date, after taking into consideration the reasons (if any) put forward by the Licence Holder for the delay.
- R3-4.2.8 Late submission gives rise to liability to an initial penalty and an additional daily penalty. If the conditions imposed by the MFSA are not met, the Authority reserves the right to take any further action as it may deem appropriate in the circumstances.

R3-4.2.9 A right of appeal to the Financial Services Tribunal is available to Licence Holders on whom penalties are imposed.

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