
 Financial Supervision Commission (Stockbrokers) (No 2) Regulatory Code 2003

Statutory Document No. 868/03



INVESTMENT BUSINESS ACTS 1991 TO 1993

FINANCIAL SUPERVISION COMMISSION (STOCKBROKERS) (No.2) REGULATORY CODE 2003

Approved by Tynwald on 09 December 2003

Coming into operation on 01 January 2004

In exercise of the powers conferred on the Financial Supervision Commission (“the Commission”) by section 6 of the Investment Business Act 1991¹ (“the Act”), and of all other enabling powers, the following Regulations are hereby made: -

**PART I
APPLICATION AND GENERAL PROVISIONS**

CITATION, COMMENCEMENT, REVOCATION AND APPLICATION

Citation and Commencement

1. (1) This Code may be cited as the “Financial Supervision Commission (Stockbrokers) (No.2) Regulatory Code 2003” and shall come into operation on 1st January 2004.

Revocation

(2) The Financial Supervision Commission (Stockbrokers) Regulatory Code 2003² and the Financial Supervision Commission (Stockbrokers) Regulatory Code 1996³ are revoked.

Application

(3) This Code applies only to holders of Category 5 investment business licences issued under Section 3 of the Act.

Interpretation

Note

A Guidance Note appended to a paragraph gives guidance as to how the Commission considers it would operate in particular circumstances. It is not part of the Code.

2. In this Code –

associate in relation to a person, means:

¹ 1991 c.18

² SD813/03

³ SD 156/96

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- (a) an undertaking in the same group as that person; and
- (b) any other person whose business or domestic relationship with the first person or its *associate* might reasonably be expected to give rise to a community of interest between them which may involve a conflict of interest in dealings with third parties.

approved bank

means, in relation to a bank account of a *firm*:

- (a) where the account is opened in the Isle of Man:
 - (i) at a bank licensed under the Banking Act 1998⁴, as amended; or
 - (ii) at a building society authorised under section 2 or as applied by section 4A of the Building Societies Act 1986⁵, as amended;
- (b) where the account is opened in the United Kingdom:
 - (i) the Bank of England;
 - (ii) the central bank of a member state of the OECD;
 - (iii) an institution with a Part IV permission under *FSMA* which includes accepting deposits and
 - (iv) a building society authorised under the Building Societies Act (of Parliament) 1986 which offers, unrestrictedly, banking services; or
- (c) where the account is opened elsewhere:
 - (i) any bank which is a subsidiary or parent company of such a bank in (b) above; or
 - (ii) a credit institution established in a EEA state and duly authorised by the relevant supervisory authority.
 - (iii) A bank which is regulated in the Channel Islands; or
- (d) a bank supervised by the South African Reserve Bank
- (e) any other bank that:
 - (i) is subject to regulation by a national banking regulator;
 - (ii) is required to provide audited accounts;
 - (iii) has minimum net assets of £5 million (or its equivalent in any other currency at the relevant time) and has a surplus revenue over expenditure for the last two financial years; and
 - (iv) has an annual audit report which is not materially qualified.

approved bank bond

means any instrument, by whatever name called, provided by an approved bank which:

- (a) provides for the immediate payment of a stated sum to the firm on demand whether by the firm or the Commission;
- (b) provides that the bank shall have no recourse to the assets of the firm in respect of the bond and that no other person shall have recourse to the assets of the firm arising in respect of the bond, until payment in full of all other creditors;
- (c) prohibits the bank from terminating the bond unless:

⁴ 1988 c.16

⁵ 1986 c.7

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- (i) the beneficiary will have financial resources equal to at least 120% of its financial resources requirement after termination or;
- (ii) the bank receives authority from the Commission to do so;
- (d) prohibits any automatic early termination of the bond whether arising out of any act or default of the firm or otherwise; and is approved by the Commission.

approved depository is any depository approved by the Commission.

approved exchange is any exchange approved by the Commission.

BCD Regulations means regulations under the Banking Consolidation Directive – the European Council Directive of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions.

call option means an option to buy an *investment* other instrument, foreign currency or physical commodity at a given price on or before a given date.

Category 5 This category is divided into three groups:

Licenceholders

- (a) Group (a) An Isle of Man branch of a firm of stockbrokers which is authorised by the Financial Services Authority.
- (b) Group (b) A firm of stockbrokers acting in the capacity of an agency broker which is not authorised by the Financial Services Authority.
- (c) Group (c) A firm of stockbrokers, other than an agency broker, acting in the capacity of a broad scope firm and is not authorised by the Financial Services Authority.

Guidance note

Agency broker means a firm which deals as principal on an incidental basis only.

Broad scope firm means a firm which deals as an agency broker but also deals as principal on more than an incidental basis.

clearing firm means a firm which assumes primary responsibility (including legal liability) for the execution and settlement of transactions for clients.

client bank account means:

- (a) an account at an approved bank which:
 - (i) is in the name of the *firm*;
 - (ii) includes in its title an appropriate description to distinguish the money in the account from the firm's money; and
 - (iii) is a current or a deposit account (or, if the *approved bank* is a building society, is a deposit (and not a share) account); or
- (b) a money market deposit of client money at an *approved bank* which is identified as being client money.

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<i>Client Money and Assets Codes ('CMA')</i>	means Part III codes 119 to 154
<i>client settlement money</i>	<p>means client money held or received by a <i>firm</i>:</p> <p>(a) for the purpose of settling:</p> <p>(i) a transaction relating to an <i>investment</i> falling within any of paragraphs 1 to 6 of Schedule 2 to <i>the Order</i>; or</p> <p>(ii) a transaction relating to an <i>investment</i> falling within any of paragraphs 7, 8 and 9 of Schedule 2 to <i>the Order</i> not being one under the terms of which the client will or may be liable to make deposits in cash or collateral to secure performance of obligations which he may have to perform when the transaction falls to be completed or upon the earlier closing out of his position; or</p> <p>(b) as a consequence of such a transaction having been settled; or</p> <p>(c) as a consequence of the discharge of any obligation by the <i>firm</i> to any other person to make a payment in connection with such a transaction in addition to settlement thereof.</p>
<i>client transaction account</i>	in relation to a <i>firm</i> and an exchange or clearing house or an <i>intermediate broker</i> , means an account maintained by the exchange, clearing house or the intermediate broker, as the case may be, in respect of <i>margined transactions</i> undertaken by the <i>firm</i> with or for its clients.
<i>Commission</i>	means the Isle or Man Financial Supervision Commission.
<i>Conduct of Business Codes ('COB')</i>	means Part IV codes 155 to 206.
<i>controller</i>	has the meaning as defined in section 10 (6) of the Act.
<i>CRR</i>	means the Counterparty Risk Requirement set out in codes 110 to 118.
<i>dealer</i>	means a person who by way of business enters into an investment agreement with the investor
<i>designated client bank account</i>	<p>means a <i>client bank account</i> with the following characteristics:</p> <p>(a) the account holds the money of one or more customers;</p> <p>(b) the account includes in its title the word "designated"</p> <p>(c) the customers whose money is in the account have each consented in writing to the use of the <i>approved bank</i> with which the client money is to be held;</p> <p>Note: In the event of the default of that bank, the account is not intended to be pooled with any other account or type of account.</p>
<i>designated client fund account</i>	<p>is one whose characteristics are:</p> <p>(a) the account holds at least part of the client money of one or more customers each of whom has consented to such money being held in the</p>

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same client bank accounts at the same banks (the client money of such clients constituting a “Designated Fund”); and

- (b) the account includes in its title the words “designated fund”.

A Designated Client Fund Account may be used for a client only where that client has consented to the use of that account and all other designated client fund accounts which may be pooled with it. A client who consents to the use of bank A and bank B must have his money held in a different designated client fund account at bank B from a client who has consented to the use of banks B and C.

Note: In the event of the default of a bank with which part of a designated fund is held, each Designated Client Fund Account held with the defaulting bank is intended to form a pool with any other Designated Client Fund Account containing part of that same Designated Fund.

eligible custodian

means:

- (a) in the case of safe custody investments which are the property of a non-private customer (other than a person who is a non-private customer under code 160 (1), any person whom the *firm* reasonably believes to be a person whose business includes the provision of *investment* custodial services; and
- (b) in the case of all other safe custody investments:
- (i) an *approved bank*;
 - (ii) an *approved depository*;
 - (iii) a regulated *clearing firm*;
 - (iv) a member of an exchange approved by the Commission ; or
 - (v) a person approved by *the Commission* for the purposes of acting as a custodian of safe custody investments.

eligible nominee

means,

- (a) an individual chosen by the customer who is not known by the *firm* to be an associate of the *firm*;
- (b) a nominee company; or
- (c) an institution authorised under the Banking Act 1998, as amended.

firm

means a holder of a Category 5 licence issued by the *Commission*

Financial Codes ('FC')

means Part II codes 27 to 118

FRA

means forward rate agreement, i.e. an agreement in which two parties agree on the payment by one party to another of an amount of interest based on an agreed interest rate for a specified period from a specified settlement date applied to an agreed principal amount; no commitment is made by either party to lend or borrow the principal amount; their exposure is only the interest difference between the agreed and actual rates at settlement.

FSA

means the United Kingdom Financial Services Authority.

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<i>FSMA</i>	means the Financial Services and Markets Act (of Parliament) 2000.
<i>General Codes ('GC')</i>	means Part I codes 3 to 26
<i>intermediate broker</i>	in relation to a margin transaction, means any person through whom the firm undertakes that transaction
<i>internal control letter</i>	<p>means a written statement from the firm addressed to the Commission, stating whether or not:-</p> <ul style="list-style-type: none"> (a) the firm has received a letter from its auditor commenting on the firm's systems and internal controls as a result of his audit of the audited annual financial statements most recently submitted by the firm to the Commission; (b) any such letter from the auditor containing any recommendation to the firm to remedy any weakness in the systems and internal controls of the firm; and (c) the firm has implemented or is implementing any such recommendations, and if not, the reasons for that decision.
<i>investment</i>	has the meaning as defined in Schedule 2 of <i>the Order</i> .
<i>life policy</i>	means an <i>investment</i> falling within paragraph 10 of Schedule 2 to <i>the Order</i> .
<i>local</i>	<p>in respect of a <i>firm</i>, means a <i>firm</i>:</p> <ul style="list-style-type: none"> (a) whose investment business consists exclusively of any one or more of the following activities: <ul style="list-style-type: none"> (i) dealing for its own account on a futures or options exchange; (ii) dealing for the accounts of other members of that exchange; (iii) making a price to other members of the same exchange; or (iv) dealing for its own account in <i>investments</i> in the capacity of a customer; (b) the performance of whose contracts is guaranteed by and is the responsibility of one or more clearing firms and in relation to (i), (ii) and (iii) above by one or more of the clearing members of the same exchange; and (c) which the Commission has given prior written approval to be treated as such for the purposes of this code.
<i>margin'd transaction</i>	means a transaction effected by a <i>firm</i> with or for a client relating to an <i>investment</i> of any description referred to in paragraphs 7, 8 and 9 of Schedule 2 to <i>the Order</i> (or any right or any interest in such an <i>investment</i>) under the terms of which the <i>client</i> will or may be liable to make a deposit in cash or collateral to secure performance of obligations which he may have to perform when the transaction falls to be completed or upon the earlier closing out of his position.

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<i>the Order</i>	means the Investment Business Order 1991 ⁶ .
<i>ordinary business investor</i>	<p>means a customer who is reasonably believed to be:</p> <ul style="list-style-type: none"> (a) a statutory corporation or local authority within the meaning of Part II of Schedule 1 to <i>the Order</i> (b) a company, partnership or unincorporated association which satisfies (or which has satisfied at any time during the previous two years) any of the following size requirements. <ul style="list-style-type: none"> (i) that it is a body corporate which has more than 20 members (or is the subsidiary of a company which has more than 20 members) and it (or any of its holdings companies or subsidiaries) has a called up share capital or net assets of £500,000 or more; (ii) that it is a body corporate and it (or any of its holding companies or subsidiaries) has a called up share capital or net assets of £5 million or more; or (iii) if it is not a body corporate, it has net assets of £5 million or more; or (c) a trustee of a trust which satisfies either of the following size requirements: <ul style="list-style-type: none"> (i) that the aggregate value of the cash and investments which form part of the trust's assets (before deducting the amount of its liabilities) is £10 million or more; or (ii) that the aggregate value has been £10 million or more at any time during the previous two years; (d) any licenceholder or overseas person which does not already qualify under (a), (b) or (c) above; or (e) a company or partnership which carries on a main business which is not investment business and which enters into that transaction as an integral part of that main business.
<i>OTC</i>	means over the counter, i.e. in relation to any <i>investment</i> , an <i>investment</i> which is not traded or listed <i>on</i> exchange or an <i>approved exchange</i> .
<i>position risk reporting statement</i>	means a statement drawn up in the format specified by <i>the Commission</i> (including such additional schedules as <i>the Commission</i> directs) and prepared at the end of each calendar quarter at a date which coincides with the monthly accounting reference date.
<i>private customer</i>	<p><i>means:</i></p> <ul style="list-style-type: none"> (a) a customer who is an individual and who is not acting in the course of carrying on investment business; or (b) unless he is reasonably believed to be an <i>ordinary business investor</i>, a customer who is a <i>small business investor</i> and who is not acting in the

⁶ GC No 366/91 as amended by SD 407/00

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course of carrying on investment business.

Guidance note

A *customer* who is treated as a *non-private customer* under code 160 is not a *private customer* under this definition. A *customer* which is a partnership or trust will not be treated as an individual *customer* within (a), notwithstanding that the *trustees* or *partners* are individuals.

<i>PRR</i>	means the Position Risk Requirement set out in codes 108 and 109.
<i>qualifying deposit</i>	means a deposit which is one of the following: <ol style="list-style-type: none"> (a) balance on current account with an <i>approved bank</i>; (b) money on deposit with an <i>approved bank</i>, United Kingdom or Isle of Man local authority, member of the Finance Houses Association, stock exchange moneybroker, regulated <i>clearing firm</i>, the National Savings Bank, exchange, <i>approved exchange</i> or <i>approved depository</i> which may be withdrawn within three months; (c) money on deposit with an <i>approved bank</i> directly related to a transaction creating an offsetting liability for the <i>firm</i> or subject to an agreement with the bank allowing its use as <i>collateral</i> for a loan that may be withdrawn within three months, which relates to a liability of the same maturity and arises out of a transaction; (d) amount evidenced by a certificate of tax deposit; (e) amount evidenced by a certificate of deposit issued by a <i>regulated banking institution</i> which matures within three months, or (f) deposit of cash by way of margin with an exchange, <i>approved exchange</i>, clearing house or intermediate broker.
<i>regulated financial institution</i>	means a <i>firm</i> , or an institution which is authorised to conduct investment business involving the execution of transactions on exchanges or on securities or derivatives approved by the Commission, provided, in the case of any such institution that the firm has no reason to suppose that the institution is in breach, in any material respect, of the codes enforceable by the relevant regulator.
<i>small business investor</i>	means <ol style="list-style-type: none"> (a) a company, partnership or unincorporated association; or (b) a trustee acting for a trust which does not satisfy a size requirement enabling the company, partnership or trustee to be treated as an <i>ordinary business investor</i> and is not otherwise an <i>ordinary business investor</i> .
<i>soft commission agreement</i>	means any agreement, whether oral or written, under which a <i>firm</i> which deals in securities on an advisory basis, or in the exercise of discretion, receives goods or services in return for business put through or in the way of another person whether on a pre-paid, continuous or retrospective basis.

Guidance note

1 This definition relates only to commission generated through *customers' orders* and does not include goods and services obtained by way of principal

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transactions by the *firm*.

- 2 Neither a *soft commission agreement*, nor an arrangement for the payment of disclosable commission, is to be taken for the purposes of code 173 on *material interest* as a relationship which gives rise to a conflict of interest in relation to transactions effected under the agreement or arrangement.

a stock exchange money broker means a moneybroker which is an FSA authorised person and acts as an intermediary in the gilt market

supranational organisation means any such organisation approved by the Commission.

Takeover Panel means the UK Panel on Takeovers and Mergers

USM means 'Unlisted Securities Market'

Guidance note

The Commission may, on the written application of a licenceholder, waive the provisions of a code under section 3(4A) of the Investment Business Act 1991.

GENERAL PROVISIONS

Commencement of Business

3. A licenceholder should commence business within 6 months of the date of the licence unless the Commission agrees otherwise in writing.

Disclosure of Regulator

4. A licenceholder should ensure that the identity of its regulator is disclosed in all correspondence, advertisements and other documents.

Guidance note

The following wording is suggested:

"Licensed to conduct Investment Business by the Isle of Man Financial Supervision Commission"

Disrepute

5. The nature and conduct of a licenceholder's business should not be such as may bring the Isle of Man into disrepute or damage its standing as a financial centre.

Other Regulations

6. (1) Category 5 Group (a) licenceholders are required to comply with all Regulations of the Financial Services Authority and any other Regulations binding on them in the United Kingdom pursuant to the Financial Services and Markets Act 2000 (of Parliament).

(2) Category 5 Group (b) and Group (c) licenceholders who are regulated in another jurisdiction by a regulatory body or equivalent acceptable to the Commission and with whom the Commission has entered into a Mutual Assistance Agreement are required to comply with all Regulations binding on them in their home jurisdiction.

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Indemnities against contraventions⁷

7. A firm shall not enter into any contract or arrangement which is specifically intended to indemnify or compensate it against any liabilities or consequences which will or may be incurred or arise as a result of:

- (1) any contravention which the firm will commit (or has reason to think that it may commit) of this Code; or
- (2) any action which the Commission will take (or which the firm has reason to think it may take) in relation to the firm or any of its employees.

Guidance note

A firm is not prohibited from entering into professional indemnity insurance policies, bona fide insurance contracts or other contracts or arrangements the main purpose of which is to ensure that the firm will be able to pay its debts.

Service of documents

8. (1) Service of documents referred to in this Code shall be effected by:
 - (a) post to the proper address;
 - (b) facsimile;
 - (c) delivery to the proper address
 - (d) personal service.
- (2) The proper address of any person is:
 - (a) in the case of a firm, the current address for service notified to the Commission;
 - (b) in the case of an individual, his business address or his usual or last known home address;
 - (c) in the case of a body corporate, its registered office or principal office;
 - (d) in the case of the Commission, The Financial Supervision Commission, PO Box 58, Finch Hill House, Bucks Road, Douglas, Isle of Man IM99 1DT; or
 - (e) the business address of the solicitor, if any, who is acting for that person in the matter in connection with which the service of the document in question is to be effected.
- (3)
 - (a) Where service is effected by post and the document is proved to have been posted, the document in question shall be presumed to have been delivered in the ordinary course of post and the date of service shall be construed accordingly.
 - (b) Where service is effected by facsimile, it shall be confirmed by the delivery or posting of a copy of the facsimile to the party to whom the facsimile was addressed and shall be taken to be served on the date of despatch of the facsimile.
 - (c) Where service is effected by leaving the document at the proper address of the person to be served, the document shall be taken to have been served on the date on which it was left.

Responsibility of a firm for employees

9. For the purposes of this Code anything said, done or omitted by an employee of a firm within the scope of his employment shall be taken as having been said, done or omitted by the firm.

Provision for cessation of business⁸

10. (1) Where a firm decides to withdraw from providing any investment business or related custodian services to customers, the firm must ensure that any such business which is outstanding is properly completed or is transferred to another licenceholder.

⁷ See also Code 169

⁸ For special provisions for cessation of business, see code 21

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- (2) Where the interests of customers of a firm in connection with the investment business would be significantly affected by the death or incapacity of an individual with the firm, the firm must:
- (a) make arrangements to protect the interests of those customers in that event; and
 - (b) on applying for an investment business licence and thereafter, provide the name and address, and such other details as may reasonably be requested, of a licenceholder with whom arrangements have been made for the protection of its customers.

Senior executive officers, compliance officers and finance officers

11. Every applicant for a licence must appoint persons who shall fill the position of:

- (1) senior executive officer;
- (2) compliance officer; and
- (3) finance officer,

and a firm must notify the Commission of who these persons are and appoint replacements to fill these positions as and when they become vacant in accordance with code 23. In the event that the firm is a branch, the Commission may permit these roles are to be filled by non-resident persons, code 12 will apply.

Dual Control (The "4-Eyes" Criterion)

12. Where the firm is a branch and the senior executive officer, compliance officer or finance officer roles are filled by non-resident persons, the business of the branch shall be effectively conducted on a day to day basis by at least two resident individuals. Internal procedures should be established to embody the concepts of dual control and, where appropriate, separation of functions.

GENERAL CONSENT REQUIREMENTS

Margined Transaction Business

13. A firm may not enter into margined transaction business for counterparties agreements without the prior written approval of the Commission.

Prior Consent Required - Branches and Subsidiaries

14. (1) A licenceholder should obtain the consent in writing of the Commission before establishing or acquiring a branch or subsidiary in the Isle of Man or elsewhere.
- (2) A firm must obtain the Commission's consent in writing prior to it becoming a subsidiary.

Acquisitions

15. A licenceholder should obtain the consent in writing of the Commission before acquiring 10% or more of the voting shares of another company.

Sales and Mergers

16. A licenceholder should obtain the consent in writing of the Commission before entering into any agreement to sell or to merge the whole or any part of the undertaking of the licenceholder or a third party.

General Notification Requirements

Immediate notification

17. A firm must notify the Commission immediately in writing of the occurrence of any of the following:
- (1) the breakdown of administrative or control procedures relevant to the licenceholder's investment business (including breakdowns of computer systems or other accounting problems) resulting or likely to result in failure to maintain proper records;

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- (2) any emergency arising:-
 - (a) which makes it impracticable for a licenceholder to comply with any one or more of the Regulatory Codes relating to investment business; and
 - (b) is outside the control of the licenceholder and its associates (and of its and their employees);and shall specify the steps that the licenceholder proposes to take to deal with the emergency;
- (3) the bringing of any indictment against the licenceholder or any associated entity;
- (4) the presentation of a petition for the winding up of the firm or of a company which is a subsidiary or holding company of the firm or the summoning of any meeting to consider a resolution to wind-up a firm or a company which is a subsidiary or holding company of the firm;
- (5) the application by any person for the appointment of a receiver, administrator or trustee of the firm;
- (6) the making or any proposals for the making of a composition or arrangement with creditors or any one creditor of the firm;
- (7) the imposition of disciplinary measures or disciplinary sanctions on the firm in relation to its investment business by any regulatory authority (including any investment exchange, clearing house or the Takeover Panel
- (8) the conviction of the firm for any offence under the legislation of any jurisdiction relating to banking or other financial services, building societies, companies, credit unions, consumer credit, friendly societies, insolvency, insurance and industrial and provident societies, or for any offence involving fraud or dishonesty, or the imposition of any penalties for deliberate tax evasion;
- (9) the re-registration of a firm incorporated with unlimited liability as a limited liability company;
- (10) the closure by a category 5, group (a) licenceholder of an Isle of Man branch so that that licenceholder ceases to maintain a permanent place of business in the Isle of Man;
- (11) the granting, withdrawal or refusal of an application for, or revocation of authorisation from any regulatory authority to carry on banking, investment business, insurance business or other financial services activity;
- (12) the granting or refusal of any application for, or revocation of, authorisation to carry on regulated banking, investment business, insurance business or other financial services activity in any country or territory outside the Isle of Man;
- (13) the granting, withdrawal or refusal of an application for authorisation under the FSMA;
- (14) the appointment of inspectors by any statutory or other regulatory authority to investigate the affairs of the firm
- (15) the bringing of any action against the firm under the legislation of any jurisdiction;
- (16) any matter which would be material to the requirements of the firm or any of its controllers to remain fit and proper;
- (17) any other matter which would be material to the Commission's supervision of the firm;

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The duty in (16) and (17) arises immediately the firm knows or has reasonable grounds for believing, that any of the above matters may have been or may be about to be committed;

(18) A licenceholder shall notify the Commission where it has reason to believe that a director, manager, partner, tied agent or employee of the licenceholder has been engaged in activities involving fraud.

Force majeure⁹

18. (1) If any emergency arises which:

- (a) makes it impracticable for a firm to comply with any of this Code; and
- (b) is outside the control of the firm and its associates (and of its and their employees), the firm shall not, so long as the emergency subsists and the firm is expeditiously taking all practicable steps available to it to relieve the emergency (and to achieve the same results despite it), be regarded as in breach of any of this Code to the extent that in consequence of the emergency this Code cannot practicably be complied with.

(2) The firm must notify the Commission immediately of any such emergency and of the steps which it is taking to relieve it.

Notification 28 days in advance

19. A firm must notify the Commission in writing, not less than 28 days before the change is implemented, of a change in:

- (1) the name of the firm;
- (2) any business name under which the firm carries on investment business in the Isle of Man;
- (3) the address of the registered office of the firm; and
- (4) the address of the place for service of notices or documents, if different from (c) above.

Scope of business

20. (1) A firm which proposes to carry on a type of investment business other than previously submitted to the Commission as part of its business plan should submit a revision to its business plan to the Commission not less than 28 days before beginning to carry on such business and should not implement such a change until it has received the Commission's consent in writing.

(2) Where a firm decides to stop carrying on a type of investment business previously set out in its business plan, it should notify the Commission of that decision and the reasons for it as soon as practicable.

Special provisions for cessation of business¹⁰

21. (1) A firm must notify the Commission in writing of the date on which it will cease to carry on investment business and the reasons for the cessation not less than 28 days in advance or, if this is not possible, immediately on becoming aware of the fact. The firm should provide a report detailing how the business is to be transferred or wound down including timescales etc. to demonstrate that investors will not be disadvantaged.

(2) A firm must notify the Commission immediately of any change in the person responsible for protecting the interests of the firm's customers in the event of the firm ceasing to carry on investment business.

Notification within 7 days

22. (1) A firm must give written notice within seven days to the Commission, of changes to the information originally provided to the Commission on the Personal Questionnaire relating to the person's name, good reputation or character of any persons involved in the investment business activities of the firm.

⁹ Where a firm is unable to comply with the Financial Codes because of an emergency, see also Code 59

¹⁰ See also code 10 (provision for cessation of business)

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(2) A person involved in the investment business activities of the firm must give immediate notice to the compliance officer of his firm or such other person as the firm may direct of any information which would be relevant for the purposes of (1) above.

Company Officers

23. (1) A licenceholder should inform the Commission in writing at least 21 days in advance of the proposed appointment of any new director, manager or company secretary and should inform the Commission in writing within fourteen days of the departure from office of a director, manager or company secretary.

(2) In addition, where the firm is a branch, a licenceholder should inform the Commission at least 21 days in advance of the proposed appointment of persons fulfilling the dual control roles and inform the Commission in writing within fourteen days of the departure from office of these persons (see code 12 above).

Guidance note

The Commission will require a personal questionnaire to be completed by proposed directors/managers/company secretaries. The appointment of a person who in the opinion of the Commission is not fit and proper may result in suspension or revocation of the licence.

Beneficial Interests

24. A licenceholder should by notice in writing inform the Commission within seven days of the discovery of any transfer of 5% or more of its voting shares or any lesser transfer which has a material effect on its immediate or ultimate beneficial control.

Actual or Intended Legal Proceedings

25. A licenceholder shall notify the Commission as soon as it becomes aware of any actual or intended legal proceedings against it where any amount claimed or disputed is likely to exceed the lower of:-

- (a) £50,000 (or the equivalent thereof); or
- (b) 10% of the firm's allowable financial resources.

Fraud and Dishonesty

26. A licenceholder shall notify the Commission where it has reason to believe that a director, manager, controller, dealer or employee of the licenceholder has been engaged in activities involving fraud or other dishonesty in relation to the firm's investment business.

PART II
FINANCIAL CODES

GENERAL FINANCIAL CODES**Application**

27. Codes 28 to 33 apply to all firms except they do not apply to a firm in respect of which the Financial Codes have been disapplied in their entirety.

Financial resources

28. A firm must at all times have available the amount and type of financial resources required by this Code.

Records and reporting

29. A firm must ensure that it maintains adequate accounting records and must prepare and submit such reports as are required by the Commission in a timely manner. A firm's records:

- (1) must be up to date and must disclose, with reasonable accuracy, at any time, the firm's financial position at that time;
- (2) must enable the firm to demonstrate its continuing compliance with its financial resources requirements; and
- (3) must provide the information:
 - (a) which the firm needs to prepare such financial statements and periodical reports as may be required by the Commission; and
 - (b) which the firm's auditor needs to form an opinion on any statements of the firm on which the auditor is required to report.

Internal controls and systems

30. A firm must, for the purpose of its compliance with codes on financial supervision, ensure that its internal controls and systems are adequate for the size, nature and complexity of its activities.

Ad hoc reporting

31. A firm must notify the Commission immediately if it becomes aware that it is in breach of, or that it expects shortly to be in breach of, codes 28, 29 or 30.

Auditors¹¹

32. A firm shall appoint an auditor. A firm shall make available to its auditor the information and explanations he needs to discharge his responsibilities as required by the Commission.

Professional Indemnity Insurance

33. Insurance cover appropriate to the licenceholder's business must at all times be maintained. Up to date details of the arrangements in force together with evidence of the cover should be filed with the Commission together with the Annual Compliance Review Report. The Commission should be promptly notified of any claims or changes to the arrangements as soon as they occur.

FINANCIAL RECORDS AND SYSTEMS OF INTERNAL CONTROL

¹¹ see also codes 83 to 95

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Keeping of Records**Records to be up-to-date**

34. A firm must keep accounting records in accordance with codes 35 to 46 on a continual basis so that at all times records are up-to-date or able to be brought up-to-date within a reasonable time.

Adequacy of records

35. A firm must keep accounting records in such a manner that they are sufficient to show and explain the firm's transactions and commitments (whether effected on its own behalf or on behalf of others) and in particular so that these records:

(1) disclose with reasonable accuracy the financial position of the firm at any point in time within the previous six years when the firm was licensed by Commission;

(2) demonstrate whether or not the firm is or was at that time complying with its financial resources requirement; and

(3) enable the firm to prepare within a reasonable time any financial reporting statement required by the Commission as at the close of business of any date within the previous six years when the firm was licensed by the Commission, and such that the statement complies with the requirements of this Code.

Content of records

36. A firm must ensure that its accounting records shall as a minimum contain:

(1) entries from day to day of all sums of money received and expended by the firm whether on its behalf or on behalf of others, and the matters in respect of which the receipt and expenditure takes place;

(2) a record of all income and expenditure of the firm explaining its nature;

(3) a record of all assets and liabilities of the firm including any commitments or contingent liabilities;

(4) entries from day to day of all purchases and sales of investments by the firm distinguishing those which are made by the firm on its own account and those which are made by or on behalf of others;

(5) entries from day to day of the receipt and dispatch of documents of title which are in the possession or control of the firm; and

(6) a record of all investments or documents of title in the possession or control of the firm showing the physical location, the beneficial owner, the purpose for which they are held and whether they are subject to any charge.

Guidance note

The Commission does not consider it possible to prepare an exhaustive and prescriptive list of record keeping requirements applicable to all firms. The detailed requirements will vary according to the manner in which the business is structured, organised and managed; its size; and the nature, volume and complexity of its transactions and commitments. The overriding principle, however, is that the records and systems must be adequate to fulfil the general requirements set out in codes 29 and 34 to 36.

Reconciliation of firm's balances**Reconciliation**

37. (1) A firm must reconcile all balances with banks or building societies (other than a client bank account subject to the Client Money Codes) as recorded by the firm to the balance on the statement issued by the bank or building society and must correct any difference forthwith, unless it arises solely as a result of identified differences in timing between the records of the firm and the bank or building society.

(2) A firm must reconcile all balances and positions whether carried out on or off exchange or with any counterparty and correct any differences by agreement on a timely basis.

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(3) A firm must perform reconciliations under (1) and (2) above as frequently as is appropriate for the volume of transactions on the accounts and in any event not less than once every five weeks.

Risk management and internal control**Exposure limits**

38. A firm must ensure that its accounting and other records contain details of exposure limits for trading positions, and for commitments under an adequate credit management policy, which are appropriate to the type, nature and volume of business undertaken and that the information contained in the records is capable of being summarised in such a way as to enable actual exposures to be measured readily and regularly against these limits.

Management information

39. A firm must maintain its records in a manner such that they disclose, or are capable of disclosing, in a prompt and appropriate fashion, the financial and business information which will enable the firm's management to:

- (1) identify, quantify, control and manage the firm's risk exposures;
- (2) make timely and informed decisions;
- (3) monitor the performance of all aspects of the firm's business on an up-to-date basis;
- (4) monitor the quality of the firm's assets; and
- (5) safeguard the assets of the firm, including assets for which the firm is responsible belonging to customers and other persons.

Systems of internal control

40 (1) A firm must establish and maintain at all times effective systems of internal control and must be able to describe and demonstrate the objectives and operation of the systems to its auditor, reporting accountant and the Commission.

(2) In determining the scope and nature of effective internal control, a firm must consider all relevant factors including the size of the business; the diversity of operations; the volume, size and frequency of transactions; the degree of risk associated with each area of operations; the amount of control by senior management over day to day operations; the degree of centralisation and the methods of data processing.

- (3) A firm must design its internal controls to ensure that:
- (a) all transactions and commitments entered into are recorded and are within the scope of authority of the firm entering into such transactions or commitments or the individual acting on behalf of the firm;
 - (b) there are procedures to safeguard assets and control liabilities, including assets belonging to third parties for which the firm is accountable; and
 - (c) there are measures, so far as is reasonably practicable, to minimise the risk of losses to the business from irregularities, fraud or error and to identify such matters should they occur so that prompt remedial action may be taken by management.

Nature, accessibility and retention of records**Nature of records**

41 (1) A firm may keep a record in a form other than a document or copy of a document provided that the record can be reproduced in hard printed form.

(2) Where all the records relating to a counterparty are not kept together, a firm must ensure that each location where documents relating to that counterparty are retained contains an indication that other records relating to that counterparty exist and how access to them can be obtained.

(3) A firm may accept and rely on records supplied by a third party so long as those records are capable of being and are reconciled with records held by the firm.

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(4) A firm's records must generally be in English but may be in another language if the firm has facilities for producing a translation of the record into English within a reasonable time of any request for production of such a translation being made by the Commission or the firm's auditor or reporting accountant.

Audit trail

42. A firm must record the information required by codes 34 to 45 in such a way as to enable a particular transaction to be identified at any time and traced through the accounting systems of the firm, in particular in such manner as to enable early identification of aggregates and of the particular items which have contributed to those aggregates.

Prompt access

43. A firm must ensure that all records are arranged, filed and indexed so as to permit prompt access to any particular record.

Retention of records

44 (1) A firm must keep all records required by codes 34 to 45 as well as any working papers necessary to show the preparation of any reporting statement or any other periodic return to the Commission.

(2) A firm must keep these records and working papers for a period of six years after the date on which they are first made or prepared.

(3) During the most recent of those years, a firm must keep these records and working papers either at a place where the firm carries on business or in such a manner that they can be produced at such a place within 24 hours of their being requested and after the first year in such a manner that they can be produced at a place of business of the firm within 48 hours.

Security of records

45. A firm must maintain adequate procedures for the maintenance, security, privacy and preservation of records, working papers and documents of title belonging to the firm or others so that they are reasonably safeguarded against loss, unauthorised access, alteration or destruction.

Production of records

46. A firm must produce any record, working paper or document required to be kept by codes 34 to 45 to the Commission or anyone nominated by the Commission on demand at such reasonable time and place as may be specified by the Commission or its nominee.

FINANCIAL REPORTING**General code**

47. (1) A firm must submit to the Commission the reporting statements required under this Code and such other reporting statements or supplementary information as the Commission may require.

(2) A firm must submit to the Commission the following reporting statements and information:

- (a) audited annual financial statements;
- (b) annual reporting statement;
- (c) auditor's report;
- (d) internal control letter;
- (e) annual reconciliation;
- (f) monthly reporting statement; and
- (g) unless the Commission otherwise permits, the position risk reporting statement;

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- (h) unless the Commission otherwise permits, if the firm has a subsidiary or subsidiaries, it must submit the audited accounts of each subsidiary together with its audited annual financial statements.
- (i) amount of funds under management
- (j) number of staff employed, split into investment and administration staff

Due dates for reporting statements**General code**

48. (1) A firm must submit to the Commission the required reporting statements and information by the due date specified in the table below.

TABLE 48(1) Due dates for reporting statements and information

Reporting statement	Number of reports per annum	Due date
Audited annual financial statements	1	3 months
Annual reporting statement	1	3 months
Auditor's report	1	3 months
Internal control letter	1	5 months
Annual reconciliation	1	3 months
Monthly reporting statement	12	15 business days
Position risk reporting statement	4	15 business days
Subsidiary's accounts	1	3 months
Amount of funds under management	1	With annual compliance review
Number of staff employed, split into investment and administration staff	1	With annual compliance review
Notes		
1 All dates are the number of days or months from the date as at which the reporting statement is prepared.		
2 That part of the auditor's report relating to client money must be also submitted within three months.		

(2) the Commission may at its sole discretion permit a firm to amend its due date for any particular reporting statement or type of reporting statements.

Authorised signatories

49. (1) Any reporting statement submitted to the Commission must be signed by two of the authorised signatories nominated to the Commission for this purpose, except for:

- (a) the auditor's report, which must be signed by the firm's auditor;
- (b) the audited accounts of a subsidiary of the firm and the firm's audited annual financial statements.

(2) Unless the Commission otherwise provides prior written approval, an authorised signatory must be a director.

Electronic reporting

50. Unless the Commission otherwise permits, a firm must submit electronic reporting statements.

NOTIFICATION

Form of notification

51. (1) A firm must effect any notification under codes 52 to 65 in writing and signed as required under (2) below, unless otherwise stated.

(2) If a firm effects a notification without writing, the firm must confirm it in writing signed by a director, senior executive officer or compliance officer (as appropriate) as soon as practicable thereafter.

Breach of financial resources

52. A firm must notify the Commission by telephone or facsimile or other equivalent means as soon as the firm has reason to believe that it is or will be in breach of the duty to have adequate financial resources. Such notification should be accompanied by details of the steps which the firm is taking, or has taken, to remedy or prevent the breach.

Deficiency in subsidiary

53. A firm must notify the Commission as soon as it has reason to believe that there is a deficiency of net assets in a subsidiary and must notify the Commission further when it believes that a deficiency no longer exists.

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Contingencies and financial commitments

54. A firm must, unless otherwise agreed with the Commission, notify the Commission as soon as it becomes aware of:

- (1) any guarantee, indemnity and other such commitment given by the firm of an amount which could give rise to a claim under 56 below;
- (2) any financial commitment (such as a guarantee) given in respect of the firm by another member of the firm's group in favour of an exchange, approved exchange or clearing house; and
- (3) any change in information previously submitted to the Commission concerning (1) or (2) above.

Failure to comply with obligations etc

55. A firm must notify the Commission as soon as it has reason to believe that it will be unable to:

- (1) submit a financial reporting statement as required by codes 47 to 50; or
- (2) make a payment to an exchange, approved exchange, clearing house or intermediate broker by the due date as required under the rules of an exchange, approved exchange or clearing house thereby causing the default of the firm under those rules.

Claims under a contingency

56. Subject to code 17(15), a firm must notify the Commission as soon as it becomes aware of any claim under a contingency made in writing by or against the firm where any amount claimed or disputed is likely to exceed the lower of:

- (1) £100,000; or
- (2) 10% of the firm's financial resources.

Misleading reporting statement

57. A firm must notify the Commission as soon as it has reason to believe that any reporting statement previously supplied by it to the Commission was or has become misleading in any material respect.

Claim on insurance policy

58. A firm must notify the Commission as soon as it makes a claim on an insurance policy it holds relating to professional indemnity or any other policy required by the rules of an exchange, approved exchange or clearing house to which it is subject.

Emergencies

59. A firm must notify the Commission if any emergency arises (such as a failure in its accounting system), unless the firm has notified the Commission under code 18, which means that the firm is unable to comply with the Financial Codes, and must specify the steps that the firm proposes to take to deal with the emergency.

Departure from accounting principles and codes

60. If it appears to a firm that there are special reasons for departing from any of the requirements in codes 66 to 81 in preparing the firm's audited annual financial statements, a firm must give particulars of the departure, the reasons for it and its effect in a note submitted with the audited annual financial statements.

Changes in accounting reference dates

61. A firm must notify the Commission as soon as it decides to make any change in its annual or monthly accounting reference dates as follows:

- (1) a firm must complete and submit to the Commission upon its request a schedule of reporting dates (an example of which can be obtained from the Commission);

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(2) a firm must provide at least 10 business days notice to the Commission of any change of annual or monthly accounting reference dates; and

(3) any change of accounting reference date outside the limits in the table below requires the prior written approval of the Commission.

TABLE 61 (3) Limits for any minor date changes

Accounting reference date	Number of days
Annual	14
Monthly	4

Guidance note

The annual accounting reference date means the date at which the audited financial statements are prepared. The monthly accounting reference date means the date at which the monthly financial statements are prepared.

Fall in financial resources

62. A firm must notify the Commission as soon as its financial resources fall below 110% of its financial resources requirement and as soon as its tangible net worth falls by 10% from the figure shown on its most recent financial reporting statement.

Qualification of audit report

63. A firm must notify the Commission as soon as it has been informed that the firm's auditor is likely to qualify his report on any audited annual financial statements of the firm.

Reconciliation of clients' money and assets

64. A firm must notify the Commission where it is unable to comply with any prescribed reconciliation requirements.

Variation of Capital

65. A licenceholder should obtain the consent in writing of the Commission before seeking to reduce or change the nature of its issued capital, or the rights and obligations of shareholders.

FORM AND CONTENT OF FINANCIAL REPORTING STATEMENTS

Agreement with records

66. A firm must prepare the financial reporting statements form, and ensure that they are in agreement with, the books and records of the firm.

True and fair

67. A firm must prepare the financial reporting statements so as to give a true and fair view of the result for the period, the financial position and state of affairs of the firm.

Offsetting or netting

68. A firm may offset amounts on the balance sheet and profit and loss account in the financial reporting statements in respect of items representing assets or income against amounts in respect of items representing liabilities or expenditure only in the case of balances with counterparties where the parties to the transaction have expressly agreed that they shall be settled on a net basis for the same value date.

Consolidation

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69. A firm must not consolidate the accounts of a separately incorporated body corporate within the group into the figures of a firm's financial reporting statements, but must include the assets, liabilities, income and expenditure of all branches of the firm.

Greater detail

70. A firm may show any item required to be shown in a financial reporting statement of a firm in greater detail than required by the appropriate format.

Items not otherwise covered

71. A firm must show as a separately identified item appended to a financial reporting statement any item representing or covering the amount of any asset or liability, income or expenditure not otherwise covered by any of the items on the required format of the statement.

Reporting currency

72. A firm's reporting currency on a financial reporting statement must be sterling unless otherwise agreed by the Commission, and a firm must not change its reporting currency without the prior written approval of the Commission.

ACCOUNTING POLICIES**General code**

73. Unless otherwise provided in this Code, a firm must determine amounts included in respect of items shown in a firm's financial reporting statements in accordance with this Code and the accounting principles and rules which the firm would apply to comply with accounting principles generally accepted in the United Kingdom and Isle of Man, subject to code 74 below.

Substance over legal form

74. A firm must include items in its financial reporting statements in such a way as to reflect the substance and not merely the legal form of the underlying transactions and balances.

Trade date accounting

75. A firm must use trade date accounting.

Doubtful debts and liabilities

76. A firm must promptly, and the Commission may require it to, make adequate provision for doubtful debts and accrue for all liabilities.

Provision for taxation

77. A firm must make adequate provision for both current and deferred taxation.

Securities lending

78. A firm may not lend securities without the prior written approval of the Commission.

Repurchase and reverse repurchase agreements etc

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79. A firm may not enter into repurchase and or reverse repurchase agreements without the prior written approval of the Commission

Foreign currency

80. A firm must translate assets and liabilities denominated in currencies other than the reporting currency into the reporting currency using the closing mid market rate of exchange, or, where appropriate, the rates of exchange fixed under the terms of related or matching forward contracts.

Valuation of positions

81. A firm must value a position on a prudent and consistent basis, as well as having regard to the liquidity of the instrument concerned and any special factors which may adversely affect the closure of the position.

A position must be valued at its close out price (close out price means that a long position shall be valued at current bid price and a short position at current offer price).

APPOINTMENTS AND DUTIES OF AUDITORS**Application**

82. Codes 83 to 95 apply to all category 5 licenceholders unless specifically exempted.

Appointment¹²

83. A firm must appoint an auditor who is qualified in accordance with code 85 below.

Auditor's Professional Indemnity Insurance

84. An auditor is not properly qualified to act as an auditor of a licenceholder unless he is covered by Professional Indemnity Insurance of not less than £10 million.

Qualification of an auditor

85. Subject to code 86 below, a person is qualified for appointment as the auditor of a firm if he is a member of one of the following bodies:

- (1) The Institute of Chartered Accountants in England and Wales;
- (2) The Institute of Chartered Accountants of Scotland;
- (3) The Institute of Chartered Accountants in Ireland; or
- (4) The Chartered Association of Certified Accountants.

Persons not qualified as auditors

86. A person is not qualified for appointment as auditor of a firm if he is:

- (1) an officer or employee of the firm;
- (2) a controller of the firm;
- (3) a person who is a partner of, or in the employment of, any person listed in (1) and (2) above;
- (4) any individual whose close relative is one of the persons listed in (1) to (3) above; or
- (5) a body corporate of which the firm or a connected company of the firm or any person listed in (1) to (4) above is a shareholder.

Change of auditors

87. A firm may change its auditor only after prior written approval by the Commission.

¹² see also code 32

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Notification of vacancy

88. Where a vacancy occurs in the office of auditor and a firm fails to appoint a replacement under this Code within four weeks of the vacancy occurring, the firm must give written notice of that fact to the Commission forthwith.

DUTIES OF AUDITOR**Engagement letter**

89. A firm must ensure that its auditor appointed under this Code has his rights and duties set out in a written engagement letter which is signed by the firm and by its auditor.

Rights and duties of the auditor

90. A firm must ensure that the engagement letter gives its auditor the rights and duties set out below:

(1) a right of access at all times to the accounting and other records of the firm and all other documents relating to its business;

(2) a right to require from the firm such information and explanations as it thinks necessary for the performance of its duties as auditor;

(3) a duty to submit a report to the Commission on the reporting statements prepared in accordance with this Code and stating the matters laid down in code 91;

(4) a duty, in preparing the report to the Commission under (3) above, to carry out such investigations as the auditor considers necessary in order to form an opinion as to the matters required to be stated in the report;

(5) a duty to submit a letter to the firm commenting on internal controls or that he has no comments, whichever is appropriate;

(6) a duty to afford to any reporting accountant all such assistance as he may require; and

(7) a duty to include with any qualification of the auditor's report to the Commission a statement specifying the relevant Commission requirements and the reasons why the opinion is qualified.

(8) a firm must retain a copy of the engagement letter required under this Code.

Content of auditor's report to the Commission

91. A firm must ensure that the auditor's report to the Commission is signed by the auditor and contains the matters specified in the table below.

TABLE 91 Contents of the auditor's report to the Commission

1	The auditor's report must be addressed to the Commission.
2	The auditor's report must state whether the auditor has: <ul style="list-style-type: none"> (a) audited the audited annual financial statements of the firm in accordance with auditing standards; (b) carried out such other procedures as are considered necessary having regard to the Auditing Practices Board's Practice Note "Investment Businesses"; and (c) obtained all the information and explanations which to the best of his knowledge and belief, are necessary for the purposes of his report to the Commission.
3	The auditor's report must also state whether in the opinion of the auditor:

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<p>(a) the audited annual financial statements of the firm give a true and fair view:</p> <p>(i) in the case of the annual balance sheet, of the state of the affairs of the firm at the date at which that balance sheet was prepared;</p> <p>(ii) in the case of the profit and loss account, of the firm's profit or loss for the period to which that account relates;</p> <p>(b) the annual reporting statement of the firm has been prepared in accordance with the form, content and accounting policies required under codes 66 to 81;</p> <p>(c) the balance sheet and the profit and loss account of the annual reporting statement are in agreement with the firm's accounting records and returns;</p> <p>(d) the balance sheet of the annual reporting statement has been properly reconciled to the balance sheet of the audited annual financial statements and monthly reporting statement prepared as at the same annual accounting reference date;</p> <p>(e) the firm has correctly calculated its expenditure requirement under code 103 for the following year;</p> <p>(f) the firm's statement of financial resources and the firm's statement of financial resources requirement in its annual reporting statement have been properly prepared in accordance with this Code;</p> <p>(g) the firm has, throughout the financial year, kept accounting records in accordance with codes 34 to 36 and codes 41 to 45;</p> <p>(h) the firm has maintained throughout the year systems to enable it to comply with the Client Money and Other Assets Codes;</p> <p>(i) the firm was in compliance with the Client Money and Other Assets Codes at the date as at which the balance sheet was prepared; and</p> <p>(j) where a subsidiary of the firm is a nominee company in whose name safe custody investments of customers of the firm are registered, whether that nominee company has maintained throughout the year systems for the safe custody, identification and control of documents of title which are adequate and which include reconciliations between the records maintained (whether by the firm or the nominee company) and statements or confirmations from banks and custodians at appropriate intervals.</p>

Qualified reports

92. (1) Where the auditor's report states that one or more of the requirements of items 3(a) to (j) of Table 91 have not been met, a firm must take reasonable steps to ensure that the report includes a statement specifying the relevant requirements and the respects in which they have not been met.

(2) Where the auditor is unable to form an opinion as to whether one or more of the requirements of items 3(a) to (j) of Table 91 have been met, a firm must take reasonable steps to ensure that the report specifies those requirements and the reasons why the auditor has been unable to form an opinion.

NOTIFICATION OF APPOINTMENT, RESIGNATION OR REMOVAL OF AUDITOR

Notification

93. A firm must, within 14 days, give notice to the Commission of any appointment, removal or resignation of an auditor appointed under this Code which contains the name and address of the auditor and, in the case of appointment:

- (1) the qualifications of the auditor; and
- (2) a statement that the appointment is in accordance with codes 83 to 88.

Failure to re-appoint an auditor

94. Failure to re-appoint an auditor at the end of his term of office is taken to be removal of that auditor for the purposes of this Code.

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Statement as to reasons for resignation or removal

95. Where an auditor resigns or is removed by the firm, a firm must attach to the notice under code 93 above a statement signed by the auditor specifying either such circumstances connected with his resignation or removal as the auditor considers should be brought to the attention of the Commission, or stating that there are no such circumstances.

BASIC COMPUTATION OF FINANCIAL RESOURCES**Firms to which codes 97 to 118 apply**

96. Codes 97 to 118 apply to all category 5 licenceholders unless specifically exempted.

The basic computation

97. (1) A firm must, at all times, maintain financial resources in excess of its financial resources requirement.

(2) A firm must calculate its financial resources and its financial resources requirement in accordance with the table below and codes 98 to 118.

TABLE 97 (2) The basic financial resources calculation

Financial resources	Financial resources requirement
Capital ("A") the sum of: - ordinary share capital - preference share capital - share premium account - profit and loss account - other approved reserves Intangible assets ("B") A - B = tangible net worth ("C")	Primary requirement ("E") the sum of: - base requirement - total liquidity adjustment - charged assets - contingent liabilities - deficiencies in subsidiaries
Eligible capital substitutes ("D") the sum of: - subordinated loans - approved bank bonds	Total PRR ("F") Total CRR ("G")
C + D = financial resources	E + F + G = financial resources requirement

Tangible net worth**Calculation**

98. (1) A firm must calculate its tangible net worth in accordance with Table 97 (2), subject to (2), (3) and (4) below.

Redeemable shares

(2) A firm may include redeemable share capital as part of tangible net worth only with the prior written approval of the Commission.

Notice of redemption

(3) A firm must provide the Commission with six months written notice of redemption of any of its redeemable shares, except where the Commission otherwise permits.

Approved reserves

(4) A firm may include reserves other than retained profits as part of tangible net worth only with the prior written approval of the Commission.

Eligible capital substitutes**Calculation**

99. (1) A firm must calculate its eligible capital substitutes in accordance with Table 97 (2), subject to (2) to (7) below.

Approval of eligible capital substitutes

(2) A firm may treat a subordinated loan or an approved bank bond as an eligible capital substitute only if it is:

- (a) drawn up in accordance with the standard forms obtained from the Commission except to the extent that the Commission otherwise permits; and
- (b) signed by authorised signatories of all the parties.

Approved lenders

(3) A firm may treat a subordinated loan as an eligible capital substitute only if the lender is:

- (a) the firm's controller;
- (b) a regulated banking institution;
- (c) a regulated financial institution; or
- (d) another person approved by the Commission.

Notice of repayment and termination

(4) A firm must provide the Commission with five business days written notice of any repayment, prepayment or termination of a subordinated loan or approved bank bond, except:

- (a) when the firm's financial resources after payment of interest or principal etc would be less than or equal to 120% of its financial resources requirement, in which case a firm must obtain the prior written approval of the Commission before repayment etc of a subordinated loan etc; or
- (b) when the Commission otherwise permits.

Amounts repayable within three months

(5) A firm may treat any amount of a subordinated loan which is repayable within three months as an eligible capital substitute only with the prior written approval of the Commission.

Limit on eligible capital substitutes

(6) The total amount of eligible capital substitutes which a firm may take into account in its financial resources must not exceed four times tangible net worth.

Limit on approved bank bonds

(7) The total of approved bank bonds which a firm may treat as an eligible capital substitute must not exceed 30% of the base requirement.

Primary Requirement**General code**

100. A firm's primary requirement is the sum of the following elements:

- (1) base requirement calculated in accordance with code 101;
- (2) total liquidity adjustment calculated in accordance with code 104;
- (3) charged assets calculated in accordance with code 105;
- (4) contingent liabilities calculated in accordance with code 106; and
- (5) deficiencies in subsidiaries calculated in accordance with code 107;

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Base requirement**General code**

101. A firm's base requirement must be the highest of the following two elements:

- (1) absolute minimum requirement, calculated in accordance with code 102 or
- (2) expenditure requirement, calculated in accordance with code 103.

Absolute minimum requirement**General code**

102. A firm's absolute minimum requirement must be:

- (1) for a group (c) licenceholder: £50,000
- (2) for a group (d) licenceholder: £100,000.

Expenditure requirement**General code**

103. (1) A firm's expenditure requirement must be 1/4 of relevant annual expenditure.

Calculation of *relevant annual expenditure*

(2) Subject to (3) and (4) below, a firm must calculate its relevant annual expenditure with reference to the firm's most recent audited annual financial statements submitted to the Commission, as follows:

- (a) its total revenue; and
- (b) any loss before taxation;
less the aggregate of the following items:
 - (c) profit before taxation;
 - (d) bonuses;
 - (e) profit shares and other appropriations of profit;
 - (f) commissions shared, other than to employees, directors, half commission men;
 - (g) fees, brokerage and other charges paid to clearing houses, exchanges, approved exchanges and intermediate brokers for the purposes of executing, registering or clearing transactions;
 - (h) interest payable to counterparties;
 - (i) interest payable on borrowings to finance the firm's investment business; and
 - (j) exceptional or extraordinary items, with the prior written approval of the Commission.

Absence of audited annual financial statements

(3) If a firm does not have audited annual financial statements, it must:

- (a) where it has just commenced trading or has not been authorised long enough to have submitted audited annual financial statements to the Commission, base its relevant annual expenditure on budgeted or other accounts which it submitted to the Commission as part of its application; or
- (b) where its accounts do not represent a 12 month period, calculate relevant annual expenditure on a proportionate basis agreed by the Commission.

The Commission's power to adjust relevant annual expenditure

(4) The Commission may require a firm to adjust its relevant annual expenditure where:

- (a) there has been a significant change in the circumstances or activities of the firm; or
- (b) the firm has a material proportion of its expenditure incurred on its behalf by third parties and such expenditure is not fully recharged to the firm.

Liquidity adjustment**General code**

104. (1) A firm's total liquidity adjustment is the sum of amounts specified as liquidity adjustments below.

Intangible assets

(2) The liquidity adjustment for intangible assets is nil (these must be deducted from capital to arrive at tangible net worth under code 98).

Tangible fixed assets

(3) The liquidity adjustment for tangible fixed assets is the total net book value of such assets, with the exception of land and buildings used as security for non recourse loans or other loans which a firm must treat under (4) and (5) below.

Land and buildings used as security for non recourse loans

(4) The liquidity adjustment for land or buildings used as security for a non recourse loan is the difference between the net book value of the land or building and the loan principal outstanding, except where the loan principal outstanding is higher than the net book value in which case there is no liquidity adjustment.

Land and buildings used as security for other loans

(5) The liquidity adjustment for land or buildings used as security for loans other than non recourse loans is the difference between the net book value of the land or building and the lower of:

- (a) 85% of a professional valuation of the land and buildings (which must have been carried out in the last two years); or
- (b) the principal outstanding,
except where both (a) and (b) are higher than the net book value in which case there is no liquidity adjustment.

Investments in connected companies

(6) The liquidity adjustment for an investment in a connected company is the balance sheet value of the investment, except where the investment is a marketable investment which is not in a subsidiary, in which case there is no liquidity adjustment but such investment must be subject to the PRR codes.

Other investments

(7) Other investments have no liquidity adjustment but instead are subject to the PRR codes.

Prepayments

(8) The liquidity adjustment for a prepayment is the balance sheet value of that prepayment, except that there is no liquidity adjustment to the extent that it relates to goods and services to be received or performed in the next three months.

Debtors arising from investment business or dealing activities

(9) Debtors arising from investment business or dealing activities have no liquidity adjustment but instead are subject to the CRR codes.

Other debtors

(10) The liquidity adjustment for debtors other than debtors arising from investment business or dealing activities is the balance sheet value of the debtor, except that there is no liquidity adjustment in the following circumstances:

- (a) amounts due from connected companies which are adequately secured and are repayable within 90 days;

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- (b) unsecured amounts due at the request of the firm from a connected company which is a regulated banking institution within 90 days;
- (c) unsecured amounts due at the request of the firm from a connected company which is a regulated financial institution within seven days;
- (d) amounts receivable in respect of cash dividends declared which have been outstanding for 30 days or less from the date the dividends were due to be paid;
- (e) amounts accrued or receivable in respect of interest on marketable investments which have been outstanding for 30 days or less from the date the interest was due to be paid;
- (f) amounts receivable on value added tax which have been outstanding for 30 days or less from the date that the value added tax return was due to be received by HM Customs & Excise; and
- (g) amounts receivable on taxation other than value added tax which have been agreed with the appropriate tax authorities and have been outstanding for 30 days or less from the date that the amounts were due to be received.

Cash deposits

(11) The liquidity adjustment for a cash deposit is the balance sheet value of the deposit, except for qualifying deposits and those other deposits which are subject to code 116.

Other assets

(12) The liquidity adjustment for assets other than those specifically stated above is the balance sheet value of the asset concerned.

Charged assets**General code**

105. A firm must calculate the primary requirement for charged assets as the aggregate balance sheet value of each asset of the firm over which a third party has the right of sale or retention on default by the firm except:

- (1) to the extent of any liability of the firm plus a reasonable margin in respect of the charged asset;
- (2) where the asset is collateral for a transaction which is subject to the CRR codes; or
- (3) where the Commission otherwise permits.

Contingent liabilities**General code**

106. A firm must calculate a primary requirement for each of its contingent liabilities if the Commission so requires.

Deficiencies in subsidiaries**General code**

107. A firm must calculate the primary requirement for deficiencies in subsidiaries as an amount equal to any deficiency in shareholders' funds at any time of a subsidiary of the firm except to the extent that:

- (1) provision has already been made by the firm; or
- (2) the firm has already calculated a liquidity adjustment or CRR because the deficiency arises or partially arises out of a liability of the subsidiary to the firm.

POSITION RISK REQUIREMENT (PRR)**Application**

108. Code 109 applies to all category 5 licenceholders unless specifically exempted.

General principles of PRR

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Obligation to calculate PRR

109. A firm must calculate a minimum PRR in the following way.

Frequency of calculation

(1) A firm must be able to monitor its total PRR on an intra-day basis and must recalculate it in a full and detailed manner before executing any trade which is likely to increase it to such a level that the firm's financial resources requirement might exceed the firm's financial resources.

Marking to market

(2) A firm must mark to market its positions, whether or not on the balance sheet, in accordance with the valuation code 81 at least once every business day and more frequently as appropriate.

Non marketable investments

(3) A firm must calculate the PRR for any position which is not a marketable investment as 100% of the mark to market value of the position or, other than in respect of a derivative (whatever the nature of the underlying instrument) or off balance sheet contract when the PRR is 100% of the value of the notional position underlying the contract.

Approach to PRR calculation

(4) A firm must calculate the total PRR by multiplying all positions in marketable investments by the relevant percentage stated in the table below and summing the results.

TABLE 109 (4) Position risk requirement**A: Debt**

Debt	Maturity		
	0-2 years	2-5 years	Over 5 years
Qualifying debt security			
- fixed interest	3.5%	5.5%	9.5%
- floating rate notes	10%	10%	10%
Non-qualifying debt security			
- fixed interest	10%	20%	30%
- floating rate notes	30%	30%	30%

B: Equities

Equities traded on or under the rules of an exchange or an approved exchange (not including USM stocks in the UK)	25%
Other	100%

C: Stock positions in physical commodities

Stock positions in physical commodities associated with a firm's investment business	30% of realisable value
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D: Certain derivatives and foreign exchange

Exchange traded futures and written options	4 x initial margin requirement
OTC futures and written options	Apply the appropriate percentage shown in A, B & C above to the mark to market value of the underlying position
Purchased options	Apply the appropriate percentage shown in A, B & C above to the mark to market value of the underlying position but the result may be limited to the mark to market value of the option

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Contracts for differences	20% of the mark to market value of the contract
Foreign exchange exposure	10% of the net open long position

E: Concentrated positions

PRR on a concentrated exposure to an issuer or an issue must be calculated in accordance with the concentrated position method.

F: Other investments

Single premium unit linked bonds and units in a regulated collective investment scheme	50% of realisable value
Any other investments	100% of mark to market value of investment or underlying instrument

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Notes**Percentage**

- 1 A percentage means, unless otherwise indicated, a percentage of the mark to market value of the aggregate of the long and the short positions in the particular category.

Netting

- 2 The long or (short position) in a particular instrument is the net of any long or short positions held in that same instrument (i.e. a long position in X shares can be offset on a share for share basis against a short position in X shares) but positions in similar instruments (e.g. X shares against Y shares) cannot be offset in this way.

Stock positions in physical commodities

- 3 A stock position in physical commodities is the mark to market value of the sum of:
- (i) commodities where the full contract price has been paid;
 - (ii) work in progress and finished goods which result from the processing of commodities; and
 - (iii) raw materials which will be combined with commodities to produce a finished processed commodity.
- 4 A stock position in physical commodities is regarded as being associated with a firm's investment business if the contract associated with the physical commodity was made for investment rather than commercial purposes. Indications of this are:
- (i) the contract is exchange traded, or
 - (ii) the performance of the contract is guaranteed by an exchange, an approved exchange or a clearing house.

COUNTERPARTY RISK REQUIREMENT (CRR)**General principles of CRR****Application**

110. (1) (a) Codes 110 to 118 apply to all category 5 licenceholders unless specifically exempted.

General code

(2) A firm must calculate its total CRR on exposures to counterparties as the sum of all the amounts calculated in accordance with the codes referred to in the table below.

TABLE 110 (2) Counterparty Risk Requirement

Codes	
111	Cash against documents transactions
112	Free deliveries of securities and physical commodities
113	Concentrated risk to one counterparty
114	Options purchased for a counterparty
115	Swaps, forward contracts and OTC derivatives
116	Qualifying and other deposits
117	Loans to counterparties
118	Other amounts owed to a firm arising out of investment business or investment dealing activities

Frequency of calculation

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(3) A firm must calculate its CRR at least once each business day; for the purposes of the relevant calculations the firm may use prices of investments and physical commodities as at the close of business on the previous day.

Negative amounts

(4) A firm must not include any CRR if it is a negative amount.

Instruments for which no CRR has been specified

(5) Where a firm is in doubt as to the classification of an item for the purposes of CRR, it must promptly seek advice from the Commission and until the Commission informs the firm of the correct treatment in the CRR calculation, the firm must add to its CRR the whole of the exposure on the item concerned.

Provisions

(6) A firm may reduce the exposure on which its CRR is calculated to the extent that it makes provision for a specific counterparty balance.

Connected companies

(7) For the avoidance of doubt, a firm must calculate a CRR as appropriate on exposures to or from connected companies.

Basis of valuation

(8) For the purposes of valuing instruments and physical commodities at market value in the calculation of CRR, a firm must be consistent in the basis it chooses and may use either mid market value or bid and offer prices (as appropriate).

Acceptable collateral

(9) A firm may reduce the exposure to a counterparty on which its CRR is calculated to the extent that it holds acceptable collateral from that counterparty.

Nil weighted counterparty exposures

(10) A firm may disregard any counterparty exposure calculated in accordance with codes 111 to 118, if the counterparty is or the contract is guaranteed by or is subject to the full faith and credit of a sovereign government or province or state thereof (or a corporation over 75% owned by such government, province or state), which is a member of the OECD and the government, province, state or corporation has not defaulted, or entered into any rescheduling or similar arrangement, or announced the intention of so doing, in respect of itself or its agency's debt within the last five years.

Cash against documents transactions**General code**

111. (1) A firm which enters into a transaction on a cash against documents basis must calculate the market risk for transactions still unsettled 16 calendar days after settlement date as set out in (2) below and must then multiply this by the appropriate percentage set out in the table below to calculate a CRR for each separate unsettled transaction.

TABLE 111 (1) Percentage to be applied to the *market risk*

Calendar days after settlement day	Percentage
0 - 15	Nil
16 - 30	25%
31 - 45	50%

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46 - 60	75%
Over 60	100%

Market risk calculation

- (2) (a) Where a firm has neither delivered securities nor received payment when purchasing securities for, or selling securities to, a counterparty, the market risk is the excess of the contract value over the market value of the securities.
- (b) Where a firm has neither received securities nor made payment when selling securities for, or purchasing securities from, a counterparty, the market risk is the excess of the market value over the contract value of the securities.

Sub-total

(3) The sum of the amounts calculated in accordance with (1) and (2) above is the firm's total CRR for cash against documents transactions.

Free deliveries of securities**General code**

112. (1) When a firm makes delivery to a counterparty of securities without receiving payment or pays for securities without receiving the certificates of good title, the firm must calculate the free delivery value for each transaction.

Free delivery value calculation

(2) A firm must calculate the free delivery value for each transaction as set out below and multiply this value by the appropriate percentage in Table 112 (2) for free deliveries of securities as follows -

- (a) if the firm has delivered securities to a counterparty and has not received payment, the free delivery amount is the full amount due to the firm (i.e. the contract value);
- (b) if the firm has made payment to a counterparty for securities and not received the certificates of good title, the free delivery amount is the market value of the securities.

TABLE 112 (2) Percentage to be applied to free deliveries relating to securities

Nature of counterparty to whom free delivery is made		Business days since delivery		
		0- 3	4 - 15	over 15
1	A counterparty to whom securities have been delivered or to whom payment for securities has been made	Nil	100% of contract or market value	100% of contract or market value
2	A regulated financial institution or regulated banking institution to whom securities have been delivered or payment made with the expectation that market practice will result in a settlement day longer than three days from delivery date		15% of contract or market value	100% of contract or market value
2A	A counterparty to whom securities have been delivered which settle through the Crest or to whom payment for such securities has been made.		15% of contract or market value	100% of contract or market value
3	A Manager, underwriter, sub-underwriter or member	nil		100% of contract or

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	of a selling syndicate or issuer to whom payment for securities has been made; or a manager of a regulated collective investment scheme to whom units of the scheme have been delivered or payment for units of the scheme has been made.		market value or, if the issue is a country approved by the Commission, , 15% of contract or market value.
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Sub-total

(4) The sum of the amounts calculated in accordance with (1) and (2) above is the firm's total CRR for free deliveries of securities.

Concentrated risk to one counterparty**General code**

113. (1) When the total amount due to a firm arising from exchange traded variation margins from a single counterparty (or several counterparties grouped together by the firm for margin or credit treatment) is outstanding under a credit line granted in accordance with an adequate credit management policy and exceeds 25% of the firm's financial resources, the firm must calculate an additional CRR according to the table below.

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TABLE 113 (1) Concentrated risk percentages

% of financial resources exposed to counterparty	Standard CRR for variation margin	Standard CRR for free delivery	Additional CRR
0 - 25%	10%	15%	nil
25% - 50%	10%	15%	lower of (1) the excess or (2) the sum of 15% for variation margin plus 10% for free deliveries
over 50%	10%	15%	lower of (1) the excess or (2) the sum of 40% for variation margin plus 35% for free deliveries

Use of approved bank bonds

(2) If an approved bank bond forms a part of a firm's financial resources, a firm may include it in financial resources for the purposes of (1) above at its face value.

Sub-total

(3) The sum of the amounts calculated in accordance with (1) above is the total CRR for concentrated risk to one counterparty.

Options purchased for a counterparty**Single premium options**

114. (1) Where a firm has purchased a single premium option on behalf of a counterparty and the counterparty has not paid the full option premium cost by three business days after trade date, a firm must calculate a CRR as the amount by which the option premium owed to the firm exceeds the market value of the option or acceptable collateral.

Traditional options

(2) Where a firm has purchased a traditional option for its own account or a counterparty and paid the option premium, it must calculate a CRR equal to the value of the option premium.

Sub-total

(3) The sum of the amounts calculated in accordance with (1) and (2) above is the firm's CRR in respect of purchased options.

Swaps, forward contracts and OTC derivatives**General code**

115. (1) A firm which has an exposure arising from the OTC instruments listed in Table 115 (1) must calculate a CRR by multiplying the credit equivalent amount by the credit percentage contained in Table 115 (3).

TABLE 115 (1) Credit equivalent amount

OTC instruments	Credit equivalent amount	
	If A is positive	If A is negative
Interest rate swaps: single currency		
(1) floating rate swapped against floating rate	A	nil

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(2)	fixed rate swapped against floating rate:		
	(a) under one year to maturity	A	nil
	(b) over one year to maturity	A + 0.5% of N	0.5% of N
Cross currency swaps			
(1)	under one year to maturity	A + 1% of N	1% of N
(2)	over one year to maturity	A + 5% of N	5% of N
FRAs, futures, purchased or written options, and other contracts for differences based solely on interest rates			
(1)	under one year to maturity	A	nil
(2)	over one year to maturity	A + 0.5% of N	0.5% of N
Futures, purchased or written options, and other contracts for differences based wholly or partly on exchange rates, commodity prices and equity prices			
(1)	contracts under 14 days original maturity	nil	nil
(2)	under one year to maturity	A + 1% of N	1% of N
(3)	over one year to maturity	A + 5% of N	5% of N
Notes			
1	A = (a) the market risk of the contract;		
	(b) in the case of a purchased option, the market value of the option; or		
	(c) in the case of a written option, the excess of contract value over market value.		
	N = the notional or actual amount underlying the contract		
2	Written options		
	Where the premium on a written option has been received within three business days from trade date, the credit equivalent amount shall be zero.		

Credit equivalent amount

(2) A firm must calculate the credit equivalent amount in accordance with Table 115 (1).

Credit percentages

(3) A firm may opt to calculate the CRR using the highest available credit percentage in the table below in order to avoid undue complication.

TABLE 115 (3) Credit percentages

Status of the counterparty		%
1	A firm, a supranational organisation, a United Kingdom discount house, a gilt edged market maker, a stock exchange money broker, a regulated banking institution, a building society under the Building Societies Act 1986, an Isle of Man or United Kingdom local authority, a investment business licenceholder and other firms which have regulations applied to them which, in the opinion of the Commission, are adequate	2%
2	Any other counterparty.	5%

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Netting

(4) A firm which has offsetting exposures in exactly the same type of contract with a counterparty may net these by novation before calculating the CRR if it has a written agreement evidencing a legally enforceable right to do so.

Equivalent contracts

(5) This Code also applies to contracts which, although they are exchange traded and related to the value of an exchange traded security or other index, are fully dependent upon the issuer for performance (e.g. covered warrants).

Regulated connected companies

(6) Where a firm carries out significant swaps business with a connected company which has, in the opinion of the Commission, adequate regulation applied to it, the firm may, with the prior written approval of the Commission, disapply all or part of this Code so far as it applies to interest rate or foreign exchange swaps with that connected company.

Timing

(7) A firm must calculate a CRR equal to 100% of the credit equivalent amount in respect of amounts due to the firm for periodic or final settlement of transactions covered by this Code which remain outstanding three business days after the due date.

Sub-total

(8) The sum of the amounts calculated in accordance with this Code is the firm's CRR for swaps, forward contracts and OTC derivatives.

Qualifying and other deposits**General code**

116. (1) Subject to (2) below, a firm must calculate a CRR for a deposit referred to in the table below by multiplying the value of the deposit by the appropriate percentage contained in the table below.

TABLE 116 (1) Qualifying and other deposit risk percentages

Type of deposit	%
Qualifying deposits	nil
Other deposits with an approved bank related to a transaction creating an offsetting liability for the firm or subject to an agreement with the bank allowing its use as collateral for a loan that may be withdrawn within:	
- three months to one year	2.5%
- over one year	4.0%
Note: all other deposits are subject to a liquidity adjustment (see code 104)	

Timing

(2) All qualifying and other deposits outstanding three days after a repayment request has been made or more than three days past maturity date are subject to a full CRR.

Sub-total

(3) The sum of the amounts calculated in accordance with Table 116(1) is the firm's CRR for qualifying deposits and other deposits.

Loans to counterparties**General code**

117. (1) A firm must calculate a 100% CRR on the amount by which a loan to a counterparty is not:
- (a) secured by acceptable collateral; or
 - (b) offset against an amount owed by the firm to the counterparty within three months where there is an agreement in writing which the firm believes to be legally enforceable, entered into by an official authorised by the debtor, allowing the firm to set off amounts owed by it against debt due to it.

Sub-total

- (2) The sum of the amounts calculated in accordance with this Code is the firm's CRR for loans to counterparties.

Other amounts owed to a firm arising out of investment business or investment dealing activities**Nil CRR items**

118. (1) The following receivables arising out of investment business or regulated dealing activities do not require a CRR at any time (see also code 104):
- (a) any debt not covered elsewhere in the CRR codes to the extent that it is adequately secured;
 - (b) amounts in respect of 30 day items specified in (3) below which have been outstanding for less than 30 days from the date on which they were first recorded on the firm's balance sheet; and
 - (c) accrued income for interest on marketable investments, except where it has been outstanding for more than 30 days after the date that the interest was due to be received.

CRR on amounts owed to a firm in respect of international underwriting and stabilisation activities

- (2) (a) Where management or other fees are owed to a firm in respect of international underwriting or stabilisation activities, the firm must calculate full CRR on any amounts remaining unpaid 30 days after they first appeared on the firm's balance sheet.
- (b) A firm acting as stabilising manager must also calculate a CRR equal to 100% of any income accrued as a result of net profit on stabilising activities while the stabilising account remains open.

CRR on 30 day items

- (3) A firm must calculate a 100% CRR in respect of the following receivables due to the firm if they have been outstanding for more than 30 days from the date on which they were first recorded on the firm's balance sheet:
- (a) commissions and fees earned in connection with the firm's investment business;
 - (b) commissions and fees earned which are due and payable from client bank accounts;
 - (c) repayments of marketable investments at maturity or call;
 - (d) the value of scrip issues and rights issues;
 - (e) proceeds arising from takeovers and mergers;
 - (f) domestic underwriting or stabilisation fees; and
 - (g) accrued income and work in progress.

100% CRR items

- (4) A firm must calculate a 100% CRR in respect of other receivables arising from investment business and investment dealing activities not covered elsewhere in this Code from the time that the receivable is recorded on the balance sheet.

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Sub-total

(5) The sum of the amounts calculated in accordance with this Code is the CRR for other amounts owed to the firm arising out of investment business or investment dealing activities.

PART III
CLIENT MONEY AND ASSETS CODES

Safekeeping**Safeguarding of customers' investments and assets**

119. (1) A firm which has custody of a customer's investments in connection with or with a view to investment business must:

- (a) keep safe, or arrange for the safekeeping of, any documents of title relating to them;
- (b) ensure that any registerable investments which it buys or holds for a customer in the course of investment business are properly registered in his name or, with the consent of the customer, in the name of an eligible nominee; and
- (c) where title to investments is recorded electronically, ensure that customer entitlements are separately identifiable from those of the firm in the records of the person maintaining records of entitlement.

Application

- (2) (a) The safekeeping codes apply to the investment business of a firm.
- (b) Where a firm holds investments on behalf of an affiliated company, it must not treat the investments as safe custody investments and apply the safekeeping codes in respect of such investments unless the affiliated company is being treated as an arm's length customer.
- (c) A firm may apply to the Commission for permission to treat safe custody investments received or held in the course of carrying on investment business, other than in the Isle of Man, in accordance with the relevant local requirements rather than the safekeeping codes.

Provision of Safe Custody facilities**Customer Notification**

120. Before a firm provides safe custody facilities to or receives collateral from a customer, it must notify the customer in writing of the obligations which the firm will have to the customer in relation to:

- (1) registration of safe custody investments and collateral if these will not be registered in the customer's name;
- (2) claiming and receiving dividends, interest payments and other rights accruing to the customer;
- (3) exercising conversion and subscription rights;
- (4) dealing with takeovers, other offers or capital re-organisations;
- (5) exercising voting rights; and
- (6) the extent of the firm's liability in the event of a default by an eligible custodian.

Registration of investments

121. (1) A firm must register registerable safe custody investments in the name of the customer, unless the customer is otherwise notified in accordance with code 120 in which case it shall be registered in the name of:

- (a) an eligible nominee which is:
 - (i) an individual, nominated by the customer, who is not an associate of the firm;
 - (ii) a nominee company controlled by either the firm or an affiliated company;
 - (iii) a nominee company owned by a recognised or designated investment exchange; or
 - (iv) a nominee company controlled by an eligible custodian;
- (b) an eligible custodian; or
- (c) with the prior written consent of the Commission, the firm itself where, due to the nature of the law or market practice of an overseas jurisdiction, it is not possible to do otherwise.

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- (2) If the firm's own investments are registered in the same name as that in which customers' safe custody investments are registered, a firm must:
- (a) register the customers' safe custody investments in a designated account different from the designated account in which the firm's investments are registered; and
 - (b) hold, if applicable, separate certificates evidencing title for the investments belonging to the firm and for customers' safe custody investments.
- (3) A firm must hold safe custody investments in the case of both registered and bearer investments:
- (a) in the physical possession of the firm;
 - (b) with an eligible custodian in a fungible account in the name of the firm designated for customers' investments; or
 - (c) with an eligible custodian in a safe custody account designated for customers' investments.

Where a firm is responsible for the recording of the safe custody investments of an affiliated company that is not being treated as an arm's length customer within the system of the Central Moneymarkets Office, such safe custody investments of the affiliated company must not be commingled in an account containing other customers' safe custody investments and must be treated as the property of the firm for the purposes of codes (3) (a) to (c) above and 122 (1) and (2) below.

Eligible Custodian Agreement

122. (1) A firm must not lodge safe custody investments with an eligible custodian in a fungible account unless the eligible custodian has agreed in writing that:
- (a) the account is designated in such a manner that the investments credited to it do not belong to the firm or to an affiliated company that is not being treated as an arm's length customer;
 - (b) the eligible custodian is not to permit withdrawal of any safe custody investments from the account otherwise than to the firm or on the firm's instructions;
 - (c) the eligible custodian will, on request, deliver to the firm a statement (as at a date specified by the firm which is not earlier than one month before the statement is delivered to the firm) specifying the description and amounts of all the investments credited to the account; and
 - (d) the eligible custodian will not claim any lien or right of retention or sale over the investments standing to the credit of any account designated pursuant to (a) above, except to the extent of any charges relating to the administration or safekeeping of safe custody investments.
- (2) A firm must not permit an eligible custodian to hold safe custody investments other than in a fungible account, unless the eligible custodian has agreed in writing that:
- (a) safe custody investments will be held in such a manner that it is readily apparent that they do not belong to the firm or to an affiliated company that is not being treated as an arm's length customer;
 - (b) the eligible custodian is not to part with possession of any safe custody investments otherwise than to the firm or on the firm's instructions;
 - (c) the eligible custodian will, on request, deliver to the firm a statement (as at a date specified by the firm which is not earlier than one month before the statement is delivered to the firm) specifying the amount of each description of investment held by the eligible custodian for the firm, and, where it is a registered investment, the amount held in each name; and
 - (d) the eligible custodian will not claim any lien or right of retention or sale over safe custody investments except to the extent of any charges relating to the administration or safekeeping of safe custody investments.

Investments registered with Nominee companies

123. A firm must ensure that any nominee company controlled by the firm or an affiliated company in whose name safe custody investments are registered maintains accounting records in accordance with the Financial Codes in respect of those investments.

Reconciliation of Clients Assets

124. A firm (or the nominee company controlled by the firm or an affiliated company) must reconcile its books and records at least every six months by one of the methods in (1) or (2) below and promptly correct any discrepancies which are revealed.

(1) The Total Count Method is:

- (a) the physical counting and inspection of all safe custody investments, collateral and other customer's property physically held by it; and
- (b) obtaining written confirmation from third parties in respect of all safe custody investments, collateral and other customer's property held by them.

(2) The Rolling Stock Check Method is:

- (a) the physical counting and inspection of safe custody investments, collateral and other customer's property of a particular description physically held by it, provided that all descriptions of safe custody investments, collateral and other customer's property are so inspected on a rolling basis within every six month period; and
- (b) obtaining written confirmation from third parties in respect of all safe custody investments, collateral and other customer's property held by them.

(3) The Rolling Stock Check Method may only be used with the Commission's prior consent and after the receipt by the Commission of a report signed by the firm's auditors in such form as the Commission determines.

Failure to perform reconciliations

(4) A firm must notify the Commission if it has not carried out or is not able to carry out reconciliations of safe custody investments and other assets belonging to third parties or if, having done so, the firm is unable to correct any differences or deficiency as required by this Code¹³.

Statement of holdings

125. (1) A firm must, as often as necessary, or on at least one date during its financial year and not less than six months after the previous statement date, provide all customers with a statement listing all safe custody investments, collateral and other property legally or beneficially owned by customers for which the firm is accountable.

(2) Where a contract note has been issued regarding a client purchase of securities within the previous three months and there is no intention to offer a custodial service in relation to those securities, the securities need not be included on the statement in (1) above.

Holding Collateral

126. Where a firm holds collateral, it must, in addition to complying with codes 119 (2), 124 and 125 (1), comply with the requirements of the table below.

¹³ For notification requirements on *reconciliation of client money*, see code 148

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TABLE 126 Requirements of a firm holding a customer's collateral

1	The firm must take reasonable steps to ensure that the collateral is properly safeguarded. Where the firm has reasonable grounds to believe that the collateral will not be properly utilised or safeguarded by a third party, then it must withdraw the collateral from that third party unless the customer had indicated otherwise in writing.
2	The collateral must be separately identifiable from assets of the firm. In addition, the customer providing the collateral must be identifiable by the firm at all times.
3	Subject to 6 below and other than by way of safe custody, before the firm deposits the collateral with, pledges, charges or grants a security arrangement over the collateral to, a third party, it must:
	(a) properly consider the credit risk to its customer; (b) notify the customer that the collateral will not be registered in the customer's name, if this is the case; (c) in the case of a segregated client, warn him that that part of the proceeds of sale of the collateral which exceeds the amount owed by the customer to the firm will be subject, on the firm's default, to the pooling codes under the Client Money Codes and should, where necessary, explain the broad effect of this;
	(d) obtain the customer's prior written consent or satisfy itself that such prior consent has been given; (e) obtain the consents referred to in 4 and 5 below, where applicable; and (f) notify any third party holding the collateral that— (i) the collateral does not belong to the firm; and (ii) the third party must not claim any lien or right of retention or sale over the collateral except to cover the obligations to the third party which gave rise to that deposit, pledge, charge or security arrangement or any charges relating to the administration or safekeeping of the collateral.
4	The firm must have prior written consent from its customer if it proposes to return to the customer collateral other than the original collateral, or original type of collateral. This does not preclude the firm from returning cash equivalent where the collateral matures.
5	The firm must not, without prior written consent from the customer, use the collateral as collateral for: (a) the firm's own obligations; or (b) the obligations of another customer or another person.
6	A firm need not obtain prior written consent from a non-private customer under 3, 4 and 5 above if prior written notice has been given by the firm.

Guidance note**1 Joint registration**

Where a customer's registrable safe custody investments are registered in the names of both the customer and an associate or associates of the firm, the investments shall be treated as being registered in the customer's own name. However, the firm should still comply with the requirement in code 120 (1) and where the firm remains accountable for such safe custody investments, the safekeeping codes will apply.

2 Repurchase and reverse repurchase agreements, securities lending and securities borrowing, buy and sale back agreements, and sale and buy back agreements.

Where a firm has absolute title to repurchase and reverse repurchase agreements, securities lending and securities borrowing, buy and sale back agreements, and sale and buy back agreements (i.e. where the holder is given an unfettered right to deal in them), such investments will not be considered as collateral for the purposes of these codes. This will apply in the case of both principal balances and any margining where required.

NB. Prior consent is required from the Commission before undertaking such transactions.

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3 Reconciliations

The comparison of records referred to in code 124 must, where relevant, include a reconciliation of the customers' beneficial (trade date) position to the physical position by reference to unsettled trades.

4 Auditors' report

The report from auditors on rolling stock checks required under code 124(3) may take the following form—

"Report of the auditors of [name of firm] to the Commission in accordance with code 124(3) as at [date].

We have examined the firm's systems of internal control for the safe custody, identification and keeping of documents and records as at [date]. In our opinion, this system is sufficient, if properly used, to enable the firm to comply with code 124 (2)."

5 Statements to customers

A firm is only required to provide statements under code 125 to customers for whom safe custody investments, collateral or other property have been held at any time during the firm's financial year.

6

Statements should give the circumstances under which safe custody investments and other property are held, lodged or otherwise deposited. The statements need not detail the names of the custodians used, nor registration details, except to distinguish between investments registered in the customer's own name and those registered in another name. Statements must distinguish those investments and property which are being used as collateral or have been pledged to third parties from other investments and property. In the case of collateral, the market valuation at the date of the statement should also be stated.

7

Since most private customers will not be aware of the settlement position of recent bargains, they are liable to be confused if statements show client money and client settlement money as calculated under the Client Money and Other Assets Codes as well as showing the actual investments held in safe custody by the firm. Therefore, all statements to private customers must be based on trade date information as regards cash balances and safe custody. Thus, an investment purchased by a customer through or from the firm would be included on the statement from trade date, and a sale of an investment through or to the firm would be excluded from the statement from trade date.

8

"Safe custody investments and other property" in code 130 must, where relevant, include collateral, but need not include client money to the extent that this has been separately notified to the customer within one month of the statement date.

9 Collateral

A firm may obtain consent (referred to in paragraphs 3d) and 3 (e) of Table 126 generally in the customer agreement or other documentation (e.g. charge document).

Client Money**Application**

127. (1) The Client Money Codes apply to the business of a firm carried on in connection with or with a view to investment business.

(2) In the course of carrying on investment business, a firm may treat money received or held other than in the Isle of Man, in accordance with the relevant local requirements rather than the Client Money Codes, where it has obtained the Commission's prior written consent.

Money received by a firm

128. (1) Subject to codes 150 to 154, a firm must treat all money received from or on behalf of a customer in the course of carrying on investment business with or for that customer as client money.

(2) Where a firm passes client money to another person in the course of investment business, the firm must not enter into an agreement under code 150 with that other person in relation to that money or purport that the money is not client money.

Guidance note

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Where a firm undertakes a range of business (securities business and derivatives business) for a non-private customer and has separate agreements with the non-private customer differently for different types of business undertaken, the firm may treat money held on behalf of the non-private customer differently for different types of business, i.e. a firm may elect to segregate money in connection with securities transactions and not segregate (by complying with code 150 below) money in connection with derivatives transactions for one customer.

Money to be held with an approved bank

129. Where a firm holds client money on behalf of a customer, it must ensure that the money is held in a client bank account with one or more approved banks in relation to which it undertakes an appropriate and continuing risk assessment.

Guidance note

A firm owes a duty of care to its customers in deciding where to deposit client money. The risk assessment required under 129 above is intended to ensure that the risks inherent in depositing client money with banks are minimised or appropriately diversified by requiring a firm to consider carefully the bank or banks with which it chooses to deposit such money. A firm would be expected to take account (not necessarily exclusively) of the following:

- (a) the capital of the bank;*
- (b) the client money deposit as a proportion of the bank's capital and deposits;*
- (c) the credit rating of the bank (if available); and*
- (d) to the extent that the information is available, the level of risk in the investment and loan activities undertaken by the bank and its affiliated companies.*

A firm is not expected to diversify deposits of client money with more than one approved bank where the amounts are of insufficient size to warrant such diversification.

Notification to an approved bank

130. (1) When a firm opens a client bank account, the firm must give or have given written notice to the approved bank requiring the bank to acknowledge to it in writing:

- (a) that all money standing to the credit of the account is held by the firm as trustee and that the bank is not entitled to combine the account with any other account or to exercise any right of set-off or counterclaim against money in that account in respect of any sum owed to it on any other account of the firm; and
- (b) that, in accordance with code 132 the title of the account sufficiently distinguishes the account from any account containing money that belongs to the firm, and is in the form requested by the firm.

(2) In the case of a client bank account in the Isle of Man, if the approved bank does not provide the acknowledgement referred to in (1) above within twenty business days of the despatch of the notice by the firm, the firm must withdraw all money standing to the credit of the account and deposit it in a client bank account with another approved bank.

Segregation

131. (1) A firm must, except to the extent permitted by the Client Money Codes, hold client money separate from the firm's own money.

(2) Where a firm deems it prudent to do so, to ensure that its customers are protected, it may deposit its own money into a client bank account, and such money will be client money for the purposes of the Client Money Codes.

(3) Where a firm pays its own money into a client bank account on the instructions of the Commission, such money will be client money for the purposes of the Client Money Codes.

(4) A firm must not hold money other than client money in a client bank account unless it is a minimum sum required to open the account or keep it in being.

Client bank accounts – general

132. Client money must be held in one or more general client bank accounts or designated client bank accounts.

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Payment of client money into a firm's account - "alternative approach"

133. A firm is not required to pay client money into a client bank account in accordance with codes 134 (1) to (3), (4)(a) and (6)(a) below, where it has obtained the Commission's prior written consent.

Guidance note

The Commission will base its decision regarding consent on whether the firm has:

- (a) *satisfied the Commission that it has adequate systems and controls to operate this system, and*
- (b) *employed a registered manager responsible for compliance with the Client Money Codes.*

A firm which obtains consent from the Commission under this code will be able to operate an "alternative approach" to the segregation of client money. A firm will be able to receive all client money into its own bank account. The firm will also be required to pay any money to or on behalf of customers out of its own account. The firm will be required to perform the segregation calculation contained in codes 141 to 144, adjust the balance held in its client bank accounts and then "lock-up" the money in the client bank accounts until the segregation calculation is re-performed on the next business day. Also with the Commission's consent, a firm will be able to operate the "alternative approach" for some types of business (eg equities transactions) and operate the "normal" approach for other types of business (eg derivatives transactions). A firm operating under the "alternative approach" will not normally be able to operate a designated client bank account, unless it can satisfy the Commission that its procedures and systems are sufficiently robust to ensure that client money held in a designated client bank account is treated in accordance with the "normal" approach.

Payment of client money into a client bank account

134. (1) Subject to (2) to (6) below, where a firm receives client money, it must either:

- (a) pay it as soon as possible (and, in any event, no later than the next business day after receipt) into a client bank account; or
- (b) pay it out in accordance with code 135.

Guidance note

A firm may segregate client money in a different currency from that of receipt. However, if it does so, it will be obliged to ensure that the amount held is adjusted each day to an amount at least equal to the original currency amount (or the currency in which the firm has liability to its customers, if different) translated at the previous day's closing spot exchange rate. In this circumstance, a firm will be expected to segregate client money in its local or functional currency.

(2) Where client money is received by the firm in the form of an automated transfer, the firm must ensure that:

- (a) where possible, the money is received directly to a client bank account; and
- (b) in the event that the money is received directly to the firm's own account, the money is paid into a client bank account in accordance with (1) above.

(3) Where a firm receives a "mixed remittance" that is part client money and part other money, it must pay the full sum into a client bank account in accordance with (1)(a) above, but must pay the money that is not client money out of the account within one business day of the day on which the firm would normally expect the remittance to be cleared, except where the money is due to the firm in respect of fees and commissions.

(4) Where a firm is liable to pay money to a customer, either in respect of an investment agreement entered into with or for that customer in the course of the firm's investment business, or by way of interest on client money, it must as soon as possible and no later than one business day after the money is due and payable:

- (a) pay it into a client bank account in accordance with (1)(a) above; or
- (b) pay it out in accordance with code 135.

(5) Where a firm receives dividends outside the Isle of Man on behalf of its customer, it may pay that money into any bank account operated by the firm, provided that such money is distributed to the customers concerned, or paid into a client bank account in accordance with (1)(a) above as soon as possible but no later than three business days after notification of receipt.

Guidance note

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A firm should ensure that it is notified promptly of any receipt of client money. This will require regular statements from overseas depots used by the firm. The frequency of such statements will depend on the volume of business.

(6) A firm must have procedures to ensure that money received by its employees or field representatives is:

- (a) paid into a client bank account of the firm in accordance with (1)(a) above; or
- (b) forwarded to the firm,
no later than the next business day after receipt.

Discharge of fiduciary duty

135. (1) Money ceases to be client money if it is paid:

- (a) to the customer;
- (b) to a third party on the instructions of the customer;
- (c) into a bank account in the name of the customer (not being an account which is also in the name of the firm); or
- (d) to the firm itself, where it is due and payable to the firm.

(2) Where a firm draws a cheque or other payable order under (1) above, the money does not cease to be client money until the cheque or order is presented and paid by the bank.

Guidance note

Where a firm despatches a cheque to a customer in respect of a delivery versus payment transaction it need not segregate that money until the cheque is presented by the customer, unless the cheque is despatched after the three day window has expired in accordance with code 154.

(3) Where a firm makes a payment to a customer, or to a third party on the instructions of the customer, from an account other than a client bank account, the sum of money in the client bank account equivalent to the amount of that payment will not become due and payable to the firm for the purposes of code 152(1) until the customer or other party has received that payment in cleared funds.

Use of an approved bank outside the Isle of Man or the United Kingdom - notification to customers

136. (1) A firm must not hold client money on behalf of a customer in a client bank account outside the Isle of Man or the United Kingdom, unless the firm has previously disclosed to the customer in writing:

- (a) the country or territory in which the account will be held;
- (b) that the legal and regulatory regime applying to the approved bank will be different from that of the Isle of Man or the United Kingdom and in the event of a default of the approved bank, his money may be treated differently from the position which would apply if the money was held by an approved bank in the Isle of Man or the United Kingdom;
- (c) in the absence of an acknowledgement as described in code 130(1), that the bank has not accepted that it has no right of set off or counterclaim against money held in a client bank account in respect of any sum owed on any other account of the firm; and
- (d) that the customer should consider taking independent legal advice if he is concerned about the implications of (b) and (c) above.

(2) Where (1) above applied and the customer is a private customer, the firm must obtain the written consent of the customer before the money is deposited in a client bank account outside the Isle of Man or the United Kingdom, unless the private customer is ordinarily resident outside the Isle of Man and the firm believes on reasonable grounds that the customer consents but does not wish to give his consent in writing, in which case a one-way notification will suffice.

Use of an intermediate broker settlement agent or OTC counterparty outside the Isle of Man and United Kingdom - notification to customers

137. (1) A firm must not undertake any transaction for a customer that involves client money being passed to an intermediate broker settlement agent or OTC counterparty located in a jurisdiction outside the Isle of Man and United Kingdom, unless the firm has previously disclosed in writing to the customer:

- (a) that his money will be passed to such a person outside the Isle of Man or United Kingdom;

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- (b) that the legal and regulatory regime applying to the intermediate broker settlement agent or OTC counterparty will be different from that of the Isle of Man and United Kingdom and in the event of a default of the intermediate broker settlement agent or OTC counterparty his money may be treated differently from the position which would apply if the money was held by an intermediate broker settlement agent or OTC counterparty in the Isle of Man and United Kingdom; and
- (c) that the customer should consider taking independent legal advice if he is concerned about the implications of (b).

Guidance note

There is no need for a firm to make separate disclosure in relation to each jurisdiction. A general disclosure concerning money that may be held with an intermediate broker settlement agent or OTC counterparty outside the Isle of Man and UK will suffice.

(2) Where (1) above applies and the customer is a private customer, the firm must obtain the written consent of the customer before the money is passed to an intermediate broker settlement agent or OTC counterparty, except where the customer is ordinarily resident outside the Isle of Man and the firm believes on reasonable grounds that the customer consents but does not wish to give his consent in writing, in which case a one-way notification will suffice.

(3) Where a customer has notified a firm in writing prior to entering into a transaction that he does not wish his money to be passed to an intermediate broker settlement agent or OTC counterparty located in a particular jurisdiction, the firm must either:

- (a) segregate the money in a client bank account and pay its own money to the firm's own account with the broker agent or counterparty; or
- (b) return the money to, or to the order of, the customer.

Guidance note

Where a customer notifies the firm in (3) above after the transaction is undertaken the firm is expected to make best endeavours to comply with either (3)(a) or (b) where it is reasonably practical to do so.

Notification on default of an approved bank, intermediate broker settlement agent or OTC counterparty

138. A firm must notify the Commission:

- (1) as soon as it is aware of the default of any approved bank, intermediate broker settlement agent, or OTC counterparty with which it has deposited or to which it has passed client money; and
- (2) as soon as reasonably practical, of its intention regarding making good any shortfall that has arisen or may arise and the amounts involved.

Interest

139. A firm must disclose to a private customer in writing whether or not interest is payable to the private customer in respect of client money and, if so, on what terms.

Guidance note

A firm is expected to outline its policy on its payment of interest in code 139 above, but not necessarily the actual rates prevailing at any particular time (see code 173 ("customer agreements")). If a firm does not have an interest agreement with a private customer, it must pay the customer all interest earned on client money held for him.

Records and auditor's report

140. A firm must keep records¹⁴ which are sufficient to demonstrate compliance with the Client Money and Assets codes.

Appropriate amounts to be held in client money bank accounts**Daily calculation**

¹⁴ The applicable requirements are contained in codes 34 to 46 and codes 89 to 91.

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141. Each business day, a firm must ensure that the aggregate balance on its client bank accounts is, by the close of business that day, at least equal to the “client money requirement” in accordance with code 142 below as at the close of business of the previous business day.

Guidance note

1. *For the purposes of 141 above, a firm should use the values contained in its accounting records, eg cash book, rather than values contained on statements received from its banks.*
2. *A buffer may be maintained in accordance with code 131 (2). However, a firm is expected to avoid holding excess client money with intermediate brokers and OTC counterparties and is expected to hold its customers’ free money in a client bank account.*
3. *Where a firm draws a cheque on its own bank account in the situation where it is operating under the “alternative approach” allowed by code 133, it will be expected to account for those cheques that have not yet cleared under code 135 (2) when performing the calculation in code 141 above. A reasonable historic average estimate of uncleared cheques may be used to satisfy this obligation.*
4. *A firm should also take into account any amounts arising from code 135 (3).*
5. *Fees and commissions may be excluded from the calculation.*

Client money requirement

142. Subject to code 144 below, the “client money requirement” is the sum of:

- (1) the “total of customers’ credit balances”, which in turn is the sum of the “individual customer balances” calculated in code 143 below, excluding:
 - (a) “individual customer balances” which are negative (ie debtors); and
 - (b) customers’ equity balances-

Securities and other non-margined transactions

143. The “individual customer balance” for each customer is the sum of:

- (1) free money where there are no trades;
- (2) **in respect of principal deals**, sale proceeds due to the customer where the customer has delivered the investments (except that if received prior to the settlement date agreed with the customer for that trade, a firm may segregate the investments instead of the money);
- (3) **in respect of agency deals**, sale proceeds due to the customer where either the sale proceeds have been received by the firm and the customer has delivered the investments, or the firm holds the customer’s investments, (except that in both cases the firm may segregate the investments instead of the money);
- (4) **in respect of principal deals**, the cost of purchases which have been paid for by the customer but the firm has not delivered the investments to the customer (except that a firm may segregate the investments instead of the money); and
- (5) **in respect of agency deals**, the cost of purchases which have been paid for by the customer where either the firm has not remitted the money to, or to the order of, the counterparty, or the investments have been received by the firm but have not been delivered to the customer (except that a firm may segregate the investments instead of the money),

less:

 - (6) money owed by the customer in respect of unpaid purchases where delivery of such investments has been made to the customer; and
 - (7) proceeds remitted to the customer in respect of sales transactions where the customer has not delivered the investments.

Guidance note

- 1 *In code 143 (1) above, a firm:*
 - (a) *includes dividends received and interest earned and allocated to a customer in respect of client money;*

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- (b) *may deduct outstanding fees, calls, rights and interest charges in accordance with any agreement with the customer, where the firm has performed its obligations in respect of that agreement; and*
- (c) *need not include money which under code 134 (5) is not required to be segregated nor include money forwarded to the firm, in accordance with code 134 (6), but not received.*
- 2 *Where a firm chooses to “segregate investments instead of money” it must ensure that the investments are held in such a manner that the firm cannot use them for its own purposes. Segregation in this context can take many forms including the holding of customers’ investments in a nominee name and the safekeeping of certificates evidencing title in a fire proof safe. It is not the intention that the full safekeeping Codes should apply to investments held in the course of settlement.*
- 3 *The term “deliver” means, for the purposes of code 143, when control of the investment passes, eg. when transaction settles in Crest.*
- 4 *A firm should segregate the contract value of any customer purchases or sales.*

Reduced client money requirement option

144. Where, in respect of a customer, there is a positive “individual customer balance” and a negative customer’s equity balance (or vice versa), a firm may offset the credit against the debit and hence have either a smaller “individual customer balance” in code 143 above.

Failure to perform calculations

145. A firm must notify the Commission immediately if it is unable to perform the calculation required by code 141.

Reconciliations

146. (1) A firm must, as often as is necessary to ensure the accuracy of its records, and at least once in every twenty five business days, reconcile:

- (a) the balance on each client bank account as recorded by the firm with the balance on that account as set out on the statement or other form of confirmation issued by the approved bank;
- (b) the balance, currency by currency, on each client transaction account with exchanges, clearing houses, intermediate brokers settlement agents and OTC counterparties as recorded by the firm with the balance on that account as set out in the statement or other form of confirmation issued by the person with whom the account is held; and
- (c) its records of approved collateral received from customers with the statement or other form of confirmation issued by the person with whom that collateral is located.

(2) A firm must perform the reconciliations in (1) above within ten business days of the date to which the reconciliation relates.

(3) Where any difference arises on any of the reconciliations in (1) above, the firm must correct it as soon as possible, unless the difference arises solely as a result of timing differences between the accounting systems of the approved bank, exchange, clearing house, intermediate broker settlement agent or OTC counterparty and of the firm.

Failure to perform reconciliations

147. (1) A firm must notify the Commission as soon as possible where it is unable to perform any of the reconciliations required by code 146.

(2) Where a firm is unable to resolve a difference arising from a reconciliation, but one of the sets of records examined by the firm during its reconciliation indicates that there might need to be a greater amount of money in the relevant client bank accounts or approved collateral than is in fact the case, the firm must assume, until the matter is finally resolved, that that set of records is accurate and pay its own money into a client bank account and such money will be client money.

Client money reporting requirement

148. A firm which handles client money must submit monthly and annual segregated accounts reporting statement to the Commission as in the table below.

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Table 148 Segregated accounts reporting statement

Type of Statement	Due date	No. of reports per annum
Monthly	15 days	12
Annually	3 months	1
Note: all due dates are the number of business days or months from the dates at which the reporting statement is prepared.		

Mandate over a bank or building society account in the customer's own name

149. (1) A firm must establish and maintain adequate records and internal controls in respect of mandate over a bank or building society account in the customer's own name, including the following:

- (a) an up-to-date list of all such mandates and any conditions placed by the customer or by the firm's management on the use of the mandate;
- (b) internal controls to ensure that all transactions entered into using such a mandate are recorded and are within the scope of authority of the person and the firm entering into such transactions; and
- (c) internal controls over the safeguarding of the passbook or other relevant documents of the customer which minimise the risk of destruction, loss, theft, fraud or error.

(2) A firm must include any passbook or other relevant document of value of a customer held by the firm or for which the firm is accountable in the annual statement sent to that customer and in the physical count and inspection of customers' property under the safekeeping codes.

Money which is not client money**Two-way "opt out"**

150. Subject to code 151 below, money is not client money if a firm:

- (1) holds it on behalf of or receives it from a non-private customer (including a market counterparty); and
- (2) has entered into a two-way customer agreement with the customer stating that:
 - (a) his money will not be subject to the protections conferred by the Client Money Codes; and
 - (b) as a consequence, his money will not be segregated from the money of the firm, and will be used by the firm in the course of the firm's business, and he will therefore rank as a general creditor of the firm.

One-way "opt out"

151. Money is not client money if a firm in respect of investment business:

- (1) holds it on behalf of or receives it from a market counterparty, and
- (2) has sent a separate written notice stating the requirements of code 150 (2) (a) and (b) above.

Money due and payable to the firm

152. (1) Money is not client money if it is immediately due and payable to the firm for its own account.
- (2) A firm may treat fees and commissions as due and payable for the purposes of (1) above if:
- (a) they have been accurately calculated and are in accordance with a formula or basis previously disclosed to the customer by the firm;
 - (b) five business days have elapsed since a statement showing the amount of those fees and commissions has been despatched to the customer, and the firm has no reason to believe that the customer questions the sum specified; or
 - (c) the precise amount of the fees or commissions has been agreed by the customer, or has been determined by a court, arbitrator or arbiter.

Money from an affiliated company

153. Money is not client money if a firm holds it on behalf of or receives it from an affiliated company, unless the affiliated company is being treated as an arm's length customer of the firm.

Money in connection with a "delivery versus payment" transaction

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154. Money need not be treated as client money in respect of a delivery versus payment transaction where it is intended that either:

(1) in respect of a customer purchase, money from a customer will be due to the firm within one business day upon the fulfilment of a delivery obligation, or

(2) in respect of a customer sale, money is due to the customer within one business day following the customer's fulfilment of a delivery obligation, unless the delivery or payment by the firm does not occur by the close of business on the third business day following the date of the receipt of money from or delivery of investments by the customer.

PART IV
CONDUCT OF BUSINESS CODES

APPLICATION OF CONDUCT OF BUSINESS CODES**Business**

155. (1) The general application of the Conduct of Business Codes is that, as far as they relate to business, they relate to business which is investment business, and accordingly, where a code relating to business applies only in particular circumstances, the code applies only if those circumstances apply in the course of investment business.

(2) Under the Order the Conduct of Business Codes also apply to firms' dealings as principal subject to the exclusions contained in the Order.

Advertisements

156. Where the Conduct of Business Codes govern the issue of an investment advertisement then firms must follow them unless specifically exempted

Reliance on others

157. (1) A person is to be taken to act in conformity with any of the Conduct of Business Codes as to information, to the extent that he can show that he reasonably relied on information provided to him in writing by a third party whom he believed on reasonable grounds to be independent and competent to provide the information.

(2) A firm may rely on the accuracy and sufficiency of the information concerning customer which is supplied by his agent provided the firm has no reasonable ground on which to doubt the authority, honesty and reliability of either the agent or the information supplied.

(3) Any communication required under the Conduct of Business Codes to be sent to a customer may be sent to the order of the customer, so long as the recipient is independent of the firm; and there is no need for a firm to send a communication itself where it believes on reasonable grounds that this has been or will be supplied direct by another person.

Chinese walls

158. (1) Where a firm maintains an established and effective arrangement which requires information obtained by the firm in the course of carrying on one part of its business of any kind to be withheld in certain circumstances from persons with whom it deals in the course of carrying on another part of its business of any kind, then in those circumstances:

- (a) that information may be so withheld; and
- (b) for that purpose, persons employed in the first part may withhold information from those employed in the second,
but only to the extent that the business of one of those parts involves investment business.

(2) Information may also be withheld where this is required by an established and effective arrangement between different parts of the business (of any kind) of a group, but this provision does not affect any requirement to transmit information which may arise apart from the Conduct of Business Codes.

(3) Where the Conduct of Business Codes apply only if a firm acts with knowledge, the firm is not for the purposes of the Conduct of Business Codes to be taken to act with knowledge if none of the relevant individuals involved on behalf of the firm acts with knowledge.

CUSTOMERS

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Market counterparties

159. (1) Subject to (2) below, a firm may treat any of the following persons as a market counterparty:
- (a) another firm;
 - (b) a trading member of an investment exchange, but only in respect of the kinds of investments traded on that exchange, or any related derivatives;
 - (c) an overseas person which regularly deals in investments off-exchange, but only in respect of investments of that kind, or any related derivatives;
 - (d) an inter-dealer broker, but only in respect of activities undertaken as inter-dealer broker;
 - (e) as regards debt investments and money market investments:
 - (i) a country;
 - (ii) an international banking or financial institution whose members are countries (or their central banks or monetary authorities);
 - (iii) an institution with a Part IV permission under FSMA which includes accepting deposits and
 - (iv) a credit institution recognised under the BCD Regulations;
 - (f) a central bank or other monetary authority of any country.
- (2) A firm may only treat a person as a market counterparty in accordance with (1) above provided:
- (a) subject to (3) below, the firm has sent that person a written notice informing it that it is to be treated as a market counterparty without the benefit of protections afforded to customers; and
 - (b) that person has not notified the firm in writing that it does not wish to be treated as a market counterparty either generally or in respect of particular kinds of investments.
- (3) A firm is not required to send a written notice in accordance with (2)(a) above to another firm where both firms are trading members of the same investment exchange.
- (4) A firm with private customers may permit itself to be treated as a market counterparty by another firm under this code where it believes on reasonable grounds that those customers will be properly protected under this code.

Guidance note

- 1 *Where a person notifies a firm under (2)(b) that it is not to be treated as a market counterparty in respect of particular kinds of investments, it may be treated as a market counterparty in respect of all other kinds of investments as permitted by (1) above.*
- 2 *Before permitting itself to be treated as a market counterparty, a firm should take into account customer protections it will lose as a result of such treatment. Where a firm believes that it will be unable to fulfil the duties and obligations owed to its private customers under this Code, it should not permit itself to be treated as a market counterparty.*

Classes of customer

160. (1) Private customer means a customer who is:
- (a) an individual and who is not acting in the course of carrying on investment business; or
 - (b) a customer who is a corporate entity and who is not acting in the course of carrying on investment business.
- (2) Non private customer means a person who has elected in writing to be treated as a non-private customer.

Guidance note

A warning must be provided to non-private customers, pointing out that the main protections afforded by the Conduct of Business Codes are applicable exclusively to private customers, in particular the obligations in respect of:

- (a) *providing risk warnings;*

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- (b) *giving suitable advice;*
- (c) *prior disclosure of charges;*
- (d) *the requirements for customer agreements; and*
- (e) *advising on and selling packaged products.*

For the avoidance of doubt, licenceholders should point out the consequent reduction of investor protection as a result of his classification as a non-private customer.

Inducements

161. A firm must take reasonable steps to ensure that neither it nor any of its agents:

- (1) offers or gives; or
- (2) solicits or accepts,

either in the course of investment business or otherwise, any inducement which is likely significantly to conflict with any duties of the recipient (or the recipient's employer) owed to customers in connection with investment business.

Soft commission

162. (1) A firm which deals for a customer on an advisory basis or in the exercise of discretion may not so deal through a broker pursuant to a soft commission agreement unless:

- (a) the only benefits to be provided under the agreement are goods or services which can reasonably be expected to assist in the provision of investment services to the firm's customers and which are in fact so used;
- (b) the broker has agreed to provide best execution to the customer;
- (c) the firm is satisfied on reasonable grounds that the terms of business and methods by which the relevant broking services will be supplied do not involve any potential for comparative price disadvantage to the customer;
- (d) in transactions in which the broker acts as principal, the firm is satisfied that commission paid under the agreement will be sufficient to cover the value of the disclosable softing services to be received and the costs of the relevant broking services; and
- (e) adequate prior and periodic disclosure is made.

Guidance note

- 1 *Broker includes a broker dealer and a market maker.*
- 2 *Customer in (1)(b) above refers to the firm receiving goods or services under a soft commission agreement.*
- 3 *Under (1)(c) above a firm may be satisfied that the relevant broking services will be supplied without involving the potential for comparative price disadvantage to the customer if:*
 - (a) *the firm is able to monitor the individual transaction prices obtained on its behalf by the broker and is satisfied that the broker has complied with its best execution obligation; or*
 - (b) *there is no need for the firm to disclose at the time of giving the order to the broker that the commission generated by the transaction is to be allocated to the firm's softing account.*
- 4 *If neither of the provisions in paragraph 3 above can be satisfied, a firm should select a soft commission broker on the basis of the broker's ability to demonstrate independence of action within the market place. This is unlikely to be fulfilled in circumstances where the broker deals exclusively with one market maker.*
- 5 *(1)(d) above is not complied with where the broker is only part remunerated by commission, unless the commission element (which must be disclosed) constitutes the greater proportion of the remuneration.*
- 6 *A broker should set its multiple at a level which it can demonstrate would generate sufficient commission income from softing transactions to cover the costs of the soft goods or services provided, the cost of dealing and settling the associated transactions, together with the specialised softing administration. When considering whether the*

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commission is sufficient to cover the costs of services provided, the broker may have regard to the aggregate number of bargains transacted and not each individual transaction.

(2) Goods or services supplied under a soft commission agreement must reasonably be expected, and must be used, to:

- (a) assist in the provision of investment services to the firm's customers by means of:
 - (i) specific advice on dealing in, or on the value of, any investment;
 - (ii) research or analysis (about investments generally or other relevant matters); or
 - (iii) the use of computer or other information facilities;
- (b) provide custodian services relating to investments of, or managed for, customers; or
- (c) provide services relating to valuations of portfolios or the measurement of the performance of portfolios.

(3) A firm which receives goods or services under a soft commission agreement must provide, to any customer to whom it is relevant, a written statement detailing its policy in relation to soft commission agreements, either at the outset of the customer relationship or as soon as reasonably practicable after the relevant soft commission agreement is entered into.

Guidance note

Policy statements should explain generally why the firm or its associate might find it necessary or desirable to pay soft commissions, bearing in mind the practices in the markets in which it does business on behalf of its customers.

- (4) (a) A firm which receives goods or services under a soft commission agreement must provide annually, to customers to whom it is relevant, the following information in relation to the period since the last report was made, or, if no previous report has been made, since the first transaction was effected under the agreement:
 - (i) the percentage of the total commission paid by the firm under soft commission agreements;
 - (ii) the value (on a cost price basis) of goods or services received by the firm under soft commission agreements expressed as a percentage of the total commissions paid by the firm, including those not paid under soft commission agreements;
 - (iii) a summary of the goods or services received by the firm under soft commission agreements;
 - (iv) a list of the brokers who are parties to the firm's soft commission agreements; and
 - (v) a statement setting out the firm's policy in relation to soft commission agreements, or a statement that its policy has not changed since the last policy statement was given.
- (b) Where a firm directs any of its soft commission business through an associate, the information provided to customers in accordance with (4)(a) above must include any such business.
- (c) A firm is not required to provide an annual report in accordance with (4)(a) and (b) above to:
 - (i) beneficiaries of funds under the firm's management; and
 - (ii) a private customer, unless it is a small business investor, provided that the firm includes in the written policy statement provided under (3) above:
 - (A) an estimate of the percentage of its total commission that the firm reasonably expects to pay under soft commission agreements; and
 - (B) a statement that details of the firm's soft commission agreements, in accordance with (4)(a) and (b) above, will be made available to the customer on request.

(5) A firm must provide to any customer to whom it is relevant a written statement of its policy in relation to soft commission agreements promptly after any material change in that policy is made.

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(6) The disclosures under (4) above are not required in the case of a customer who is ordinarily resident outside the Isle of Man, provided the firm believes on reasonable grounds that he does not wish to receive such information.

Guidance note

- 1 *The disclosure requirement contained in (4) above applies to a firm which receives goods or services under a soft commission agreement in return for placing business through, or in the way of, another party to the agreement. The disclosure can be made on a general basis to all customers to whom it is relevant, namely any customer for whom the firm enters into transactions where the commission generated has been or is to be used to pay for goods or services received under a soft commission agreement.*
- 2 *Where goods or services obtained through a soft commission agreement have a mixed use, partly falling outside the generic description of permitted goods and services contained in (2) above, the firm should make an appropriate allocation of the costs and disclose them in accordance with (4) above. Only the percentage of the specific component or service that meets the criteria set out in (2) above may be paid for from soft commission.*
- 3 *The goods and services in the table below fall within the generic description set out in (2) above and can be offered under a soft commission agreement.*

TABLE 162 (6) A - Soft commission: permitted goods and services

research and advisory services, including economic factors and trends portfolio valuation and analysis performance measurement market price services custodian services computer hardware associated with specialised computer software or research services dedicated telephone lines seminar fees (where the subject matter is of relevance to the provision of investment services) publications (where the subject matter is of relevance to the provision of investment services) -----

This list is for indicative purposes and is not exhaustive

- 4 *The goods and services in the table below do not fall within the generic description set out in (2) above.*

TABLE 162 (6) B - Soft commission: non-permitted goods and services

travel, accommodation or entertainment costs, whether or not related to the provision of investment services any seminar fees not falling within the permitted goods and services list any subscription for publications not falling within the permitted goods and services list office administrative computer software, for example word processing, accounting programmes computer hardware not associated with specialist computer software membership fees to professional associations purchase or rental of office equipment or ancillary facilities employees' salaries direct money payments -----

This list is for indicative purposes and is not exhaustive

Issue of advertisements**General Requirements**

163. (1) An advertisement shall not contain –
 - (a) a statement, promise or forecast which is untrue or misleading;

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- (b) a statement of fact which the licenceholder does not at the time the advertisement is issued have reasonable grounds supported by documentary evidence for believing to be true;
- (c) a statement of opinion held by any person (whether the licenceholder or any other person) which the licenceholder does not at the time the advertisement is issued have reasonable grounds supported by documentary evidence for believing to be the honestly held opinion of that person at that time;
- (d) a statement of fact which the licenceholder does not at the time the advertisement is issued have reasonable grounds for believing will continue to be true for so long as it remains relevant to the subject matter of the advertisement;
- (e) a misleading statement about the scale of activities of, or any of the activities of, or the resources of or available to, the licenceholder or the licenceholder's group;
- (f) a statement relating to past performance unless:-
 - (i) the basis on which such performance is measured is clearly stated and the presentation is not exaggerated;
 - (ii) it is accompanied by a warning that past performance is not necessarily a guide to future performance; or
 - (iii) the past performance is relevant to the investment or the services offered by the licenceholder;
- (g) a statement relating to taxation benefits unless it is properly qualified to show what it means in practice and to whom such benefits apply; or
- (h) a comparison with other forms of investment unless the basis of comparison is clearly stated and the comparison is fair.

(2) The content and format of any advertisement shall not:-

- (a) be so designed as to be likely to be misunderstood;
- (b) be so designed as to disguise the significance of any warning statement or information which is required to be included under this Code;
- (c) be presented in such a way that it is not clearly identifiable as an advertisement; or
- (d) signify in any way that the advertisement is approved or has been approved by the Commission.

(3) Any advertisement shall :-

- (a) identify the person who issued it or caused it to be issued;
- (b) contain the address of the licenceholder who issued it or caused it to be issued; and
- (c) state the nature and category of any licence or authorisation under the Investment Business Act 1991 held by that person.

(4) Any advertisement issued by a licenceholder which refers to statutory compensation arrangements shall contain sufficient information to make it clear to the investor or potential investor whether such arrangements apply to him.

(5) Any advertisement issued by a licenceholder in another jurisdiction should comply with any advertising regulations or law in that other jurisdiction.

(6) In assessing whether an advertisement complies in its opinion with the spirit of the Code, the Commission will take into account matters of fact or opinion or forecasts which have been omitted (or might properly have been included) in the advertisement as well as the content and form of the advertisement itself, the

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context in which it is issued, the general impression that it creates, and the likelihood of any person being misled by it.

Requirements relating to specific investments

164. (1) An advertisement shall not specify some but not all of the terms and conditions which attach to an investment unless:-

- (a) those which are specified give a fair indication of the nature of the investment and the risks involved; and
- (b) the advertisement contains information as to how a written statement of all the terms and conditions can be obtained.

(2) Any advertisement shall disclose any special areas of risk relating to the investment, such as limited marketability.

- (a) In the case of an investment the value of which may fluctuate or is not guaranteed (or both) the advertisement shall state that fact prominently.
- (b) In the case of an investment the value of which is guaranteed the advertisement shall state clearly the nature of the guarantee and to what it relates and whether there are any matters which may affect the investor's ability to benefit from it.

(3) Any reference to income tax or other tax benefits shall include information about the tax situation of the investment/fund as well as that of the investor.

(4) An advertisement shall not specify a rate of return without specifying how it is calculated, including any element which involves any reduction of the investor's capital.

(5) An advertisement issued by a licenceholder for an investment which is governed by advertising regulations or other regulations in its country of origin/domicile shall comply with those regulations and shall contain a statement to that effect.

(6) Any advertisement issued by a licenceholder for an investment which is subject to regulation outside the Isle of Man shall contain a statement of the country or territory under whose law it is regulated and the name of the regulatory authority.

(7) Any advertisement inviting direct investment in futures, options, and contracts for differences shall contain a risk warning as follows : "The risks of loss from investing in commodity and financial futures, foreign exchange contracts, securities and index contracts and options can be substantial."

(8) A licenceholder should keep a record of all advertisements issued by it including the date of issue, the publications in which it has been included, and evidence to support any statement made in the advertisement which purports to be a statement of fact or opinion, or how access to such evidence may be obtained.

Guidance note

The Commission will generally decline to vet or approve advertisements before issue, but if, exceptionally, it does review any such advertisements, such review and the views expressed by the Commission shall not prejudice any disciplinary action or proceedings thereafter.

However, the Commission expects licenceholders to comply with the Code. The Commission will take into account in its assessment of the fitness and propriety of the licenceholders and their employees and representatives' actions and behaviour in relation to advertising which it considers deceitful or improper but which may not amount to a breach of this Regulatory Code. Before reaching any conclusions in the matter the Commission will raise it with representatives of the licenceholder and take account of any representations they may wish to make as well as their response to a request from the Commission to withdraw or amend the advertisement.

UNSOLICITED CALLS**Responsible behaviour on the telephone or on visits**

165. Licenceholders should have procedures for requiring those seeking to obtain business to be civil and considerate, not to use any undue pressure, deception or artificiality, to make plain their purpose and identity to clients and potential clients.

Standards of conduct for unsolicited calls

166. Licenceholders must observe the highest standards of behaviour at all times in making unsolicited calls.

PACKAGED PRODUCTS**Promotion of packaged products - Information about packaged products**

167. A licenceholder should ensure that before or immediately after a recommendation is made to take out a life policy or buy units in a collective investment scheme, a private investor is given or sent a statement, prepared by the recommender or by the product company, which informs him of details of the product, which should include premiums or other amounts payable then and in the future, the factors relevant to the ultimate value of the investment (or benefits payable under it), the consequence of not keeping up the payments, and any surrender or transfer value.

Guidance note

This Code does not apply where a licenceholder is acting under the terms of a discretionary management agreement.

CUSTOMER AGREEMENTS**Customer agreements**

168. (1) Where a firm provides investment services to a private customer on written contractual terms, the agreement must set out in adequate detail the basis on which those services are provided.

- (2) Where a firm provides to:
- (a) a private customer investment services involving contingent liability transactions; or
 - (b) any customer investment services involving the discretionary management of the customer's assets,

it must do so under a two-way customer agreement, unless the customer is ordinarily resident outside the Isle of Man and the firm believes on reasonable grounds that he does not wish a two-way customer agreement to be used.

A two-way customer agreement which a firm enters into with a customer in accordance with the above must set out in adequate detail the basis on which the services are to be provided and, if relevant, the extent of the discretion to be exercised by the firm.

- (3) (a) A firm must ensure that the matters referred to in the table below are included in a two-way customer agreement entered into with a customer in accordance with (2) above.

TABLE 168 (3) (a) Two-way customer agreements required contents

1	Name and registered address of the firm, or its principal address in the Isle of Man, and a statement that the firm is regulated by the Commission
2	A statement of the services to be provided
3	statement of the basis upon which the firm is to charge for its services, or a reference to a separate document which may be amended periodically
4	A statement of the customer's investment objectives except in the case of an execution-only service. (These may be included in a separate document attached to the customer agreement to which the customer's attention is drawn)
5	A statement of any restrictions on the investments which the firm may acquire for the customer or a statement that there are no such restrictions

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- (b) A firm must ensure that the appropriate matters referred to in the table below are included in a two-way customer agreement entered into with a customer in accordance with (2) above.

TABLE 168 (3) (b) Two-way customer agreements required contents if applicable

1	The extent of the discretion to be exercised by the firm
2	A statement that the firm may enter into transactions for the customer, either generally or subject to specified limitations, under which the customer will incur obligations as an underwriter or sub-underwriter
3	A statement as to whether the firm will undertake transactions with or for the customer in investments which are not on exchange or which are not readily realisable investments
4	Where the portfolio or account is not specifically established for the purpose of carrying on derivatives' business, a statement, if relevant, that the firm may enter into transactions which may result in the customer having a short position
5	A statement of the basis on which the customer will incur any contingent liability, including margining requirements, such as rights to fund margin calls and the maximum limits placed on such funding
6	A statement of the basis by which the firm may receive remuneration from another person in connection with transactions entered into for or on behalf of the customer and that the amounts of any such remuneration will be available on request
7	Where any part of the portfolio or account is to be available for investment in contingent liability transactions, the maximum amount or percentage so available
8	A statement that the firm has authority to borrow or raise money on the customer's behalf, or enter into transactions which will involve the customer having to borrow or raise money and the maximum borrowing limit must be stated
9	A statement, that the firm holds or intends to hold client money in a client bank account with an approved bank which is in the same group as the firm, identifying the bank concerned
10	A statement as to the treatment of the customer's assets by the firm, in accordance with codes 119 and 126
11	A statement concerning any custodian responsibility related to investment business accepted by the firm, including a statement that sub-custodians are connected with the firm
12	Particulars of any rights which the firm may have to realise assets (including collateral) held on behalf of the customer in satisfaction of a default by the customer or otherwise, and of any rights which the firm may have to close out or liquidate contracts or positions in respect of any of the customer's investments
13	A statement of the valuation dates on which valuations under code 185 (periodic information) will be prepared
14	A statement specifying any associates of the firm to whom the firm may delegate any of the services provided under the agreement

- (4) (a) A *firm* must not enter into a transaction with or for a *customer* unless it has received an instruction from the *customer* relating to that transaction.

- (b) (a) above does not apply where:

- (i) a *firm* provides *investment services* to a *customer* involving the discretionary management of the *customer's* assets and acts in accordance with (2) above;
- (ii) a *firm* exercises default remedies against the *customer*; or
- (iii) a *firm* closes out the *customer's* position as a result of the *customer* failing to meet a margin call

Stock lending for private customers

169. (1) A firm must not undertake stock lending activity with or for a private customer unless the customer has given his prior written consent, specifying the assets to be lent, the type and value of acceptable collateral from the borrower and the method and amount of remuneration due to the customer in respect of the lending. Prior consent from the Commission is also required.

Customers' rights

170. (1) A firm must not, in any written communication or agreement, seek to exclude or restrict any duty or liability to a customer which it has under any statute law and any code or standard (which applies to the

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licenceholder) which has been issued or endorsed by any investment exchange where investment business is conducted or by the Commission.

(2) Similarly, unless it is reasonable to do so in the circumstances, a firm must not, in any written communication or agreement, seek to exclude or restrict:

- (a) any other duty to act with skill, care and diligence which is owed to a private customer in connection with the provision to him of investment services in the course of investment business; or
- (b) any liability owed to a private customer in connection with investment business for failure to exercise the degree of skill, care and diligence which may reasonably be expected of it in the provision of investment services in the course of that business.

(3) A firm must not seek unreasonably to rely on any provision seeking to exclude or restrict any such duty or liability

(4) Without the customer's prior written consent, a firm must not execute transactions for a private customer, or effect or arrange a discretionary transaction for any customer, under which he will incur obligations as an underwriter or sub-underwriter in connection with any form of issue of investments (including any offer for subscription, any offer for sale or any placing of investments, or any takeover offer where the consideration does or may consist of investments).

(5) The consent given by the customer in accordance with (4) above may be general or related to specific issues of investments.

Default remedies

171. (1) Upon a default by a private customer, a firm must not realise other assets of that customer in satisfaction of the default unless it is legally entitled to do so, and:

- (a) prior to the default, it has given the customer written notice of the default remedies that it may exercise; or
- (b) it has given the customer notice (oral or written) of its intention to exercise such remedies at least three business days before it does so.

Customer borrowing

172. (1) A firm must not knowingly lend money or extend credit to a private customer, and must not arrange for any other person to do so unless:

- (a) the firm has made and recorded an assessment of the private customer's financial standing, based on information disclosed by that customer, and is satisfied that the arrangements for the loan or credit and the amount concerned are suitable in relation to the type of investment agreement proposed or likely to be entered into by him; and
- (c) the customer has given his prior written consent, specifying the maximum amount of the loan or credit together with details of the amount or basis of any charges to be levied in connection with the loan or credit.

(2) (1) above does not apply where a firm:

- (a) settles a securities transaction in the event of default or late payment by the customer; or
- (b) pays an amount to cover a margin call made on a private customer for a period no longer than five business days.

(3) A firm which effects a contingent liability transaction with or for a customer must:

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- (a) require the customer to provide any margin which is payable, whether at the outset or subsequently, and take reasonable care to satisfy itself that the customer is aware of the consequences of not paying it; and
- (b) monitor daily the amount of margin which must be paid by the customer, so that the aggregate amount of such margin is always covered by cash, equity balances or acceptable collateral: and, unless the firm is an approved bank which is holding a customer's money in an account with itself, where there is a shortfall, the firm must fund the difference until the shortfall is eliminated.

(4) A firm may not effect a contingent liability transaction unless it can show that it believes on reasonable grounds that the customer understands:

- (a) the circumstances under which he may be required to provide any margin;
- (b) particulars of the form in which margin may be provided;
- (c) particulars of the steps which the firm may be entitled to take if the customer fails to provide the required margin;
- (d) that failure by the customer to meet a margin call may lead to the firm closing out his position after a time limit specified by the firm, and that the firm will be required to close out the position in any event after a period of five business days; and
- (e) the circumstances, other than failure to provide margin, which may lead to the customer's position being closed out without prior reference to him.

(5) In the case of a private customer, the matters referred to in (4) above must be set out in a two-way customer agreement.

(6) Margin to be payable by the customer in respect of an on-exchange contingent liability transaction in accordance with (4)(a) above must be of an amount or value which at least equals the margin requirements of the relevant exchange or clearing house.

(7) Subject to (8) below, a firm must close out a private customer's open position, where he fails to meet a margin call after a period of five business days.

(8) A firm may make a secured or unsecured loan or grant credit to a customer for the purpose of making a deposit or required margin payment if:

- (a) a credit assessment is made on the customer by an employee of the firm who is independent of the trading or marketing functions of the firm; and
- (b) the maximum amount of the loan or credit to be granted has been notified to the customer, and in respect of a private customer has been set out in writing and agreed to by the customer in accordance with code 172.

Guidance note

In support of the requirements of code 172 (4), a firm should ensure that the customer makes appropriate arrangements with the firm for communications regarding margin calls. A customer should be made aware of the consequences of the firm being unable to contact him.

In circumstances where a two-way customer agreement is not required for contingent liability transactions with a private customer (i.e. the exception in code 168 (2), the matters referred to in code 172 (4) need not be set out in a two-way customer agreement in accordance with code 172 (5), but nevertheless must be set out in writing and consented to in writing by the non-Isle of Man private customer.

A private customer's position need not be closed out in accordance with code 172 (7) where a margin payment is outstanding after five business days where the firm has received third party confirmation that payment has been made and the firm believes on reasonable grounds that the delay is due to circumstances beyond the customer's control.

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Notification to a customer in accordance with code 172 (8) is only required when a loan is first made, or a credit line is first extended, and then only subsequently when an additional loan is made or the limit placed on the credit line is varied.

CUSTOMER RELATIONS**Material interest**

173. (1) Where a firm has a material interest in a transaction to be entered into with or for a customer, or a relationship which gives rise to a conflict of interest in relation to such a transaction, the firm must not knowingly either advise, or deal in the exercise of discretion, in relation to that transaction, unless it takes reasonable steps to ensure fair treatment for the customer.

(2) A firm may take reasonable steps to ensure fair treatment for the customer in accordance with (1) above by relying on a policy of independence. If a firm relies on a policy of independence, that policy must:

- (a) require the relevant employee or agent to disregard any material interest or conflict of interest when advising customers or dealing for them in the exercise of discretion; and
- (b) be set out in writing and known by the relevant employee or agent.

(3) Where a firm relies on a policy of independence in respect of private customers, the firm must have disclosed in writing to them that:

- (a) it may give investment advice or deal in the exercise of discretion on their behalf where it may have a material interest or conflict of interest relating to the investment, transaction or service concerned; and
- (b) the relevant employee or agent is required to comply with a policy of independence and disregard any material interest or conflict of interest when making recommendations or arranging transactions.

Guidance to (2) and (3)

Where the presence of an independence policy is not of itself sufficient to ensure fair treatment for customers, the firm should take other steps, such as specific disclosure, to ensure compliance with (1) above. Firms should also consider conflicts of interest.

(1) above prohibits the use of guaranteed stops by firms in respect of customers for whom the firm is acting as a discretionary investment manager. The conflict of interest arising would be so great that the only way in which the firm could ensure fair treatment for its customers would be to decline from entering into the transaction.

Customers' understanding

174. (1) A firm must not recommend a transaction to a private customer, or act as a discretionary manager for him, unless it has taken reasonable steps to enable him to understand the nature of the risks involved.

- (2) In respect of a warrant or derivative, before a firm
 - (a) recommends a transaction;
 - (b) arranges or executes a transaction (even if it has not recommended it); or
 - (c) acts as a discretionary manager,
 it must have sent the private customer the Warrants or Derivatives Risk Warning Notice¹⁵, and obtained a copy signed by the customer in circumstances where the firm is satisfied that the customer has had a proper opportunity to consider its terms.

(3) A firm is not required under (2) above to obtain a signed copy of the relevant risk warning notice in the case of the firm believes on reasonable grounds that he does not wish to receive it or to consent in writing.

¹⁵ For these risk warning notices see **Appendices A and B**

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(4) (2) above does not apply to realisations of warrants already held by the customer, or warrants attached to another security.

(5) A firm must not recommend to a private customer a transaction in an investment which is not a readily realisable investment unless it:

- (a) warns him of the difficulties in establishing a proper market price and, if the recommendation concerns a purchase, in making a subsequent sale; and
- (b) discloses any position knowingly held by the firm or an associate in the investment or a related investment.

Guidance note

In order to comply with (1) above, there may be circumstances in which the firm should give additional warnings or explanations to those required under (2) and (5). Examples of such circumstances include investment by a private customer in unregulated collective investment schemes or where guaranteed stops are provided by the firm in respect of derivatives transactions.

Stock lending

175. A firm undertaking stock lending activity with or for a private customer must advise the private customer that it may affect his taxation position and that he should consult his tax adviser prior to any involvement in this activity.

Guidance note

A firm which intends to carry on stock lending activity where it will borrow a customer's stock for its own account or lend a customer's stock to an associate must disclose its or its associate's interest to the customer, either generally or in respect of each transaction. The prior consent of the Commission must be sought.

Suitability

176. (1) A firm must take reasonable steps to ensure that it does not in the course of investment business:

- (a) make any personal recommendation to a private customer of an investment or investment agreement; or
- (b) effect or arrange a discretionary transaction with or for any customer, unless the recommendation or transaction is suitable for him having regard to the facts disclosed by that customer and other relevant facts about the customer of which the firm is, or reasonably should be, aware.

Guidance note

In respect of a guaranteed stop, this code requires a firm to determine whether, as an alternative to the guaranteed stop, there is an appropriate exchange traded contract that would better suit the customer's needs.

(2) But where, with the agreement of the customer, a firm has pooled his funds with those of others with a view to taking common management decisions, the firm must instead take reasonable steps to ensure that the transaction is suitable for the fund, having regard to the stated investment objectives of the fund.

(3) A firm which acts as:

- (a) an investment manager for a private customer; or
- (b) a discretionary investment manager for a non-private customer, must ensure that the customer's portfolio or account remains suitable, having regard to the facts disclosed by that customer or other relevant facts about the customer of which the firm is, or reasonably should be, aware.

Charges and other remuneration

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177. (1) The amount of a firm's charges to a private customer for the provision of investment services to him must not be unreasonable in the circumstances.

(2) Before a firm provides investment services to a private customer, it must disclose to him the basis or amount of its charges for the provision of those services

Guidance note.

(2) above requires a firm to make full disclosure to its customer of all charges associated with a guaranteed stop.

(3) The disclosure of the basis, nature or amount of any charges referred to in (2) above does not apply to any commission received from another customer as a result of a simultaneous matching transaction.

(4) Before a firm undertakes investment transactions for or advises a client, it should inform him, unless he has specifically agreed that this is unnecessary, of all relevant facts relating to its remuneration (including the remuneration of any intermediary which is payable by the client) attributable to the transaction or advice.

Confirmations and periodic information

Contract notes and confirmations

178. A firm which effects a sale or purchase of an investment (other than a life policy) with or for a customer must ensure that he is sent with due despatch a note containing the essential details of the transaction.

Contract notes (securities)

179. The note required under code 178 above must contain, in respect of the sale or purchase of a security, the details contained in the table below.

TABLE 179 Contents of contract notes

1	The firm's name and a statement that it is regulated by the Commission
2	The customer's name, account number or other identifier
3	The date of the transaction, and either the time of execution or that the customer will be notified of that time on request
4	The security concerned, the size involved and whether the transaction was a sale or purchase
5	The unit price at which the transaction was executed or averaged, and the total consideration due from or to the customer, and a statement, if applicable, that the price is an averaged price
6	The settlement date, where agreed
7	The amount of the firm's charges to the customer in connection with the transaction
8	The amount or basis of remuneration which the firm has received or will receive from another person in connection with the transaction will be made available on request
9	The amount or basis of any remuneration shared with another person (except employees), or the fact that this will be made available on request
10	If the transaction is a purchase of a unit in a collective investment scheme, the amount of any front-end-loading
11	Whether the firm executed the transaction as principal, and whether the transaction was executed with or through an associate
12	A statement, if this is the case, that any dividend, bonus or other right which has been declared, but which has not been paid, allotted or otherwise become effective in respect of the relevant security, will not pass to the purchaser under the transaction
13	If any interest which has accrued or will accrue on the relevant security is accounted for separately from the transaction price, the amount of the interest which the purchaser will receive or the number of days for which he will receive interest
14	The amount of any costs, including transaction taxes, which are incidental to the transaction and which

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	will not be paid by the firm out of the charges mentioned in 7 above
15	If the transaction involved, or will involve, the purchase of one currency with another, the rate of exchange involved or a statement that the rate will be supplied when the currency has been purchased

Confirmation notes (derivatives)

180. The note required under code 178 above must contain, in respect of the sale or purchase of a derivative, the details contained in the table below.

TABLE 180 Contents of confirmation notes

1	The firm's name and a statement that it is regulated by the Commission
2	The customer's name, account number or other identifier
3	The date of the transaction, and either the time of execution or that the customer will be notified of that time on request
4	The derivative concerned, the size involved and whether the transaction was a sale or purchase
5	The unit price at which the transaction was executed, which in the case of an option must include a reference to the last exercise date and the strike price of the option
6	The maturity, delivery or expiry date of the derivative
7	The amount of the firm's charges to the customer in connection with the transaction
8	The amount or basis of any remuneration which the firm has received or will receive from another person in connection with the transaction, or the fact that this will be made available on request
9	The amount or basis of any charges shared with another person (except employees), or the fact that this will be made available on request
10	The amount of any costs, including transaction taxes, which are incidental to the transaction and which will not be paid by the firm out of the charges mentioned in 7 above
11	If the transaction involved, or will involve, the purchase of one currency with another, the rate of exchange involved or a statement that the rate will be supplied when the currency has been purchased, including the maturity or expiry date of any currency hedge, unless such currency hedge is separately reportable under code 178 above

Difference accounts

181. The note required under code 178 above must contain, in respect of any futures transaction which closes out an open position, all details required by Table 180 above in respect of each contract comprised in the open position and each contract by which it was closed out, and the profit or loss to the customer arising out of the closing out of that position.

Exercise of options

182. When an option has been exercised by or against a customer, the note required under code 178 above must contain the details referred to in the table below.

TABLE 182 Contents of exercise notice

1	The firm's name and a statement that it is regulated by the Commission
2	The customer's name, account number or other identifier
3	The date of exercise, and either the time of exercise or that the customer will be notified of that time on request
4	The option concerned, the size involved and whether the exercise creates a sale or purchase in the underlying asset
5	The amount of all the firm's charges to the customer in respect of the exercise
6	The strike price of the option and, where applicable, the total consideration due from or to the customer
7	The amount of any costs, including transaction taxes, which are incidental to the exercise and which will not be paid by the firm out of the charges mentioned in 5 above
8	If the exercise involved, or will involve, the purchase of one currency with another, the rate of exchange involved or a statement that the rate will be supplied when the currency has been purchased

Guidance note

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For a currency option, the rate of exchange will be the same as the strike price.

General provisions and exceptions

183. (1) The details required under codes 179 to 182 above may be provided electronically.
- (2) A firm is not required to state any detail required under codes 179 to 182 above which is dependent upon information provided by other persons, if the information is not available to the firm at the time when the note is prepared; but the fact that the information is not available must be stated and a supplementary note must be sent to the customer with due despatch once the information is known by the firm.
- (3) A firm is not required to identify separately the unit price and the charges in respect of a transaction to a non-private customer who has requested a note showing a single price combining both of these items.
- (4) A firm can provide the details required under Table 179 item 15, Table 180 item 11, and Table 182 item 8 above in a separate note.
- (5) A firm is not required to send a note under code 178 above in respect of:
- (a) (i) currency, interest rate, equity or commodity swaps;
 - (ii) asset trading;
 - (iii) stock lending or borrowing transactions;
 - (iv) repurchase or reverse repurchase agreements, and
 - (v) sale or buy-back agreements,
- for a non-private customer who does not require one; and
- (b) transactions in a regulated collective investment scheme, or investment trust under an arrangement where the customer makes regular payments of previously agreed amounts provided the customer is sent a portfolio valuation in accordance with code 170 (4).
- (6) A firm may retain notes required to be sent under code 178 above for a customer who is ordinarily resident outside the Isle of Man with that customer's prior consent. Such notes must be retained by the firm's compliance officer or an employee of the firm designated by him who is not personally involved in handling the customer's portfolio or account

Averaging of prices

184. (1) (a) A firm may execute a series of transactions within a 24 hour period to achieve one investment decision or objective, or to meet orders which it has aggregated.
- (b) If the firm does so, it may determine a uniform price to the transactions executed during that period, calculated as the weighted average of the various prices of the transactions in the series.
- (c) In the circumstances in (a) above, the firm may comply with code 178 above by sending out a note relating to those transactions with due despatch after the last transaction within the relevant 24 hour period.
- (2) (a) A firm may execute a series of transactions to achieve one investment decision or objective over a period up to and including five business days with the agreement of a non-private customer.
- (b) If the firm does so, it may determine a uniform price to the transactions executed during the period, calculated as the weighted average of the various prices of the transactions in the series.

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- (c) In the circumstances in (a) above, the firm may comply with code 178 above by sending out a note relating to those transactions with due despatch after the last transaction has been completed.

(3) In transactions in respect of which the firm has calculated a weighted average price under (1) and (2) above, the firm must, nonetheless, treat each of the underlying transactions as a separate transaction for the purposes of complying with code 206 (record keeping).

Periodic information

185. (1) A firm which acts as an investment manager for a private customer or as a discretionary investment manager for a non-private customer must send a valuation report at intervals which are not less frequent than six monthly in respect of securities or securities-related cash balances as at the valuation date.

(2) Subject to (3) below, a firm must send a customer a valuation report at intervals which are not less frequent than monthly in respect of any derivatives or derivatives-related cash balances contained in the customer's account, as at the valuation date, including any pooled account in which the customer has an interest.

(3) Where a firm is not acting as the customer's investment manager, the requirement in (2) above applies only in respect of derivatives which are contingent liability investments other than:

- (a) those which the firm enters into with or for a non-private customer where the transaction is not made on exchange; and
- (b) written call options covered by the customer having the identical type and amount of the underlying instrument, or written put options covered by the customer having the cash available to meet his obligations should the option be exercised.

Guidance note

In order to rely on the exception in (3)(b) above relating to written options, a firm must be satisfied that the customer has available the necessary collateral or cash throughout the life of the option to meet his obligations free from any other encumbrance. This should be met by the customer depositing the collateral or cash with the firm or the relevant clearing house.

(4) A firm is not required to send a valuation report in accordance with (1) and (2) above where the customer:

- (a) has advised the firm in writing that he wishes to receive them less frequently (although the customer must be sent a valuation report on at least an annual basis); or
- (b) is not ordinarily resident in the Isle of Man and has given his prior consent for them to be retained by the firm's compliance officer or an employee of the firm designated by him, who is not personally involved in handling the customer's portfolio or account.

(5) A firm must send a valuation report promptly following the end of each valuation period.

Portfolio valuations (securities)

186. (1) (a) A valuation report sent in accordance with code 185 (1) above to a private customer for whom the firm is acting as an investment manager on a non-discretionary basis must include items 1 (contents and value) and 2 (basis of valuation) in the table below.
- (b) A valuation report sent in accordance with code 185 (1) above to a customer for whom the firm is managing a discretionary portfolio must include all the matters referred to in the table below.

TABLE 186 (1) Contents of portfolio valuations

1 Contents and value
(a) The number, description and value of each security held in the portfolio;
(b) the amount of cash balances (which may be shown on a separate statement); and
(c) the aggregate amount of the portfolio's value on the valuation date.
2 Basis of valuation
A statement of the basis on which the value of each security at the valuation date has been arrived at (or a reference to an earlier document containing this statement), and, if applicable, a statement that the basis for valuing a specified security has changed since the previous valuation report. Where some of the investments are shown in a currency other than the usual one used for valuing the portfolio, the relevant currency exchange rates must be shown.

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<p>3 Transactions and changes in composition</p> <p>(a) Particulars of each transaction entered into for the portfolio during the period;</p> <p>(b) the aggregate of money and particulars of all securities transferred into and out of the portfolio during the period; and</p> <p>(c) the aggregate of interest payments, dividends and other benefits received by the firm for the portfolio during the period.</p> <p>The particulars required under (a)-(c) above may be disclosed on separate statements (excluding contract notes) issued to the customer during the valuation period.</p>
<p>4 Charges and remuneration</p> <p>The portfolio valuation should inform the client, unless he has specifically agreed that this is unnecessary, of all relevant facts relating to its remuneration (including the remuneration of any intermediary which is payable by the client) attributable to the transaction or advice.</p>
<p>5 Securities pledged or charged</p> <p>(a) Particulars of any securities at the valuation date either which have been pledged by the firm as collateral, or charged by the firm to secure borrowings on behalf of the portfolio; and</p> <p>(b) the aggregate of any interest payments made during the period in respect of such loans or borrowings.</p>

Account valuations (derivatives)

187. (1) The valuation report sent to a customer in accordance with code 185 (2) above in respect of futures and related cash balances must include all the matters referred to in the table below.

TABLE 187 (1) Contents of account valuations

<p>1 Changes in value</p> <p>The aggregate of money transferred into and out of the account during the valuation period.</p>
<p>2 Closed positions</p> <p>In relation to each transaction effected during the valuation period to close out a customer's position, the resulting profit or loss to the customer after deducting or adding commission (as appropriate) in respect of that transaction. A net profit or loss may be shown in respect of the customer's overall position in each commodity rather than the profit or loss attributable to each contract.</p> <p>The particulars required in respect of closed positions may be disclosed on separate statements (excluding confirmations or difference accounts) issued to the customer during the valuation period.</p>
<p>3 Open positions</p> <p>The particulars of each open position in the account at the close of business on the valuation date showing unrealised profit or loss in respect of each position (before deducting in either case any commission which would be payable on the closing out of that position).</p> <p>A net profit or loss may be shown in respect of the customer's overall position in each commodity rather than the profit or loss attributable to each contract.</p>
<p>4 Aggregate of contents</p> <p>The aggregate of each of the following in, or relating to, the customer's account at the close of business on the valuation date:</p> <p>(a) cash;</p> <p>(b) collateral value;</p> <p>(c) management fees; and</p> <p>(d) commissions attributable to transactions during the period or a statement that this information has been separately disclosed in writing on earlier statements or confirmations to the customer.</p>

(2) The valuation report sent to a customer in accordance with code 185 (2) above in respect of options and related cash balances must include items 1 (changes in value) and 4 (aggregate of contents) referred to in the table above, and the matters referred to in the table below.

TABLE 187 (2) Additional contents of options account valuations

<p>Open positions</p> <p>In respect of each open option contained in the account on the valuation date</p>

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- (a) the share, future, index or other investment or asset involved;
- (b) the trade price and date for the opening transaction;
- (c) the market price of the contract;
- (d) the exercise price of the contract; and

Options account valuations may show an average trade price and market price in respect of an option series where the customer purchases a number of contracts within the same series.

Item (b) may be omitted in valuation statements following the statement for the period in which the option was opened.

Periodic information for broker funds

188. (1) A firm managing investments in a broker fund must send to a private customer at no less than six monthly intervals a periodic statement containing, to the extent that the firm can reasonably be expected to obtain it, the information in the table below.

TABLE 188 (1) Contents of periodic statement for broker funds

1	The value of the units at the start of the period and on the valuation date
2	A description of any asset where the value totals more than 5% of the total asset value of the fund including a statement of the percentage value
3	The aggregate value of the commission, benefits and other remuneration received by the firm or paid to a third party during the period
4	The investment objectives and strategies including an indication if either of these have changed since the previous report
5	Where the fund consists of a unit-linked policy and unless the firm is managing a broker fund on behalf of a single customer, a comparison over the reporting period and over a period beginning with the date on which the fund was created of the percentage change in the price of the units in the fund against the percentage change over the same period: <ul style="list-style-type: none"> (a) in the case of a fund which is dedicated to pension policies, the prices of units in the managed unit-linked pension fund of the life office; and (b) in the case of a fund which is not dedicated to pension policies, the prices of units in the managed unit-linked life fund of the life office; in either case where there is more than one managed unit-linked pension fund or unit-linked life fund, the fund which the firm believes on reasonable grounds to be the most suitable comparator
6	Unless the firm is managing a broker fund on behalf of a single customer, a comparison of the price of units in the fund or scheme with the published index or sector average stated in the product particulars

(2) A firm managing investments in a broker fund which has a life policy linked to it must provide to the customer on an annual basis (coinciding with the date the life policy was issued) to the extent that the firm can reasonably be expected to obtain the following information:

- (a) the date the life policy was issued;
- (b) the number of units in the fund allocated to the policy holder's life policy;
- (c) the offer price of these units; and
- (d) the realisable value of these units.

(3) A firm is not required to provide the customer with the periodic information set out in (1) and (2) above where it believes on reasonable grounds that the life office or scheme operator will provide the same information direct to the customer.

CUSTOMER DEALING**Dealing ahead of publications**

189. (1) Subject to (2) below, where a firm or its associate intends to publish to customers a written recommendation, or a piece of research or analysis, it must not knowingly effect an own account transaction in

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the investment concerned or any related investment until the customers for whom the publication was principally intended have had (or are likely to have had) a reasonable opportunity to react to it.

- (2) A firm may effect an own account transaction if:
- (a) the publication could not reasonably be expected materially to affect the price of the investment concerned or any related investment;
 - (b) the firm is a market maker in the investment concerned or in a related investment and the transaction is effected by it in good faith in the normal course of market making;
 - (c) the firm deals in order to fulfil an unsolicited customer's order;
 - (d) the firm believes on reasonable grounds that it needs to deal to fulfil customers' orders which are likely to result from the publication, and that its doing so will not cause the price of the investment which is the subject of the written recommendation, or piece of research or analysis, to move against customers' interests by a material amount; or
 - (e) the firm or its associate discloses in the publication that it or its associate has effected or may effect an own account transaction in the investment concerned or any related investment.

Customer order priority

190. (1) A firm must deal with customer and own account orders fairly and in due turn.

Timely execution

191. (1) Once a firm has agreed or decided in its discretion to effect or arrange a current customer order, it must effect or arrange the execution of the order as soon as reasonably practicable in the circumstances.

(2) But (1) above does not preclude a firm from postponing execution of an order where it believes on reasonable grounds that this is in the best interests of the customer.

Best execution

192. (1) Where a firm deals with or for a private customer, it must provide best execution.

(2) A firm must also provide best execution where it fulfils an order from a non-private customer, unless the customer has waived this requirement.

Timely allocation

193. (1) A firm must ensure that a transaction it executes is promptly allocated.

- (2) The allocation must be:
- (a) to the account of the customer on whose instructions the transaction was executed;
 - (b) in respect of a discretionary transaction, to the account of the customer or customers with or for whom the firm had made and recorded, prior to the transaction, a decision in principle to execute that transaction; or
 - (c) in all other cases, to the account of the firm.

Aggregating orders

194. (1) A firm may aggregate an order for a customer with orders for other customers, or with own account orders, where:

- (a) it is unlikely that the aggregation will operate to the disadvantage of any of the customers whose orders have been aggregated; or
- (b) the firm has disclosed to the customer that his order may be aggregated and that the effect of the aggregation may operate on some occasions to his disadvantage.

Guidance note

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A firm should only aggregate customers' orders where it believes on reasonable grounds that this is in the overall best interests of its customers.

Fair allocation

195. (1) Where a firm has aggregated an order for a customer transaction with an order for an own account transaction, or with another order for a customer transaction, then in the subsequent allocation:
- (2) it must not give unfair preference to itself or to any of those for whom it dealt; and
 - (3) if all cannot be satisfied, it must give priority to satisfying orders for customer transactions unless it believes on reasonable grounds that, without its own participation, it would not have been able to effect those orders either on such favourable terms or at all.

Churning and switching

196. (1) A firm must not:
- (a) make a personal recommendation to a private customer to deal; or
 - (b) deal or arrange a deal in the exercise of discretion for any customer, if the dealing would reasonably be regarded as too frequent in the circumstances.
- (2) A firm must not:
- (a) make a personal recommendation to a private customer to switch within a packaged product or between packaged products; or
 - (b) effect such a switch in the exercise of discretion for a private customer, unless it believes on reasonable grounds that the switch is justified from the customer's viewpoint.

Certain derivatives transactions to be on exchange

197. A firm must not effect, arrange or recommend a contingent liability transaction with, for or to a private customer unless:

- (1) the transaction is made on exchange; or
- (2) the firm believes on reasonable grounds that the purpose of the transaction is to hedge against currency risk involved in a position which the customer holds.

Off-exchange market makers

198. Where a firm sells to a private customer any securities which are not quoted on a recognised or designated investment exchange, whilst giving the customer the impression that the firm is a market maker in the security concerned, it must:

- (1) give notice to the customer that it is required to ensure that a reasonable price for repurchase of the security is available to him for a specified period which must not be less than three months after the date the notice is given; and
- (2) ensure that such a price is available to him for that specified period.

MARKET INTEGRITY**Insider dealing**

199. (1) A firm must not effect (either in the Isle of Man or elsewhere) an own account transaction when it knows of circumstances which mean that it, its associate, or an employee or agent of either, is prohibited from effecting that transaction by the statutory restrictions on insider dealing.

(2) A firm must use its best endeavours to ensure that it does not knowingly effect (either in the course of investment business or otherwise) a transaction for a customer it knows is so prohibited.

- (3) But (1) and (2) above do not apply where:

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- (a) the prohibition applies only because of knowledge of the firm's own intentions;
- (b) the firm is a recognised market maker with obligations to deal in the investment; or
- (c) the firm is a trustee or personal representative who acts on the advice of a third party appearing to be an appropriate adviser who is not so prohibited.

Stabilisation of securities

200. Firms may not undertake stabilisation without the prior written permission of the Commission and such permission may be accompanied by licence conditions.

Reportable transactions

201. (1) A firm must make available to the Commission, in accordance with, and subject to, the provisions below, details about transactions (including own account transactions) in investments which it effects.

(2) A firm which is party to a transaction must report to the Commission any transaction falling within the scope of the Commission, except for the following kinds of investments or transactions:

- (a) public or municipal debt issued or guaranteed by the governments or government agencies of Japan or United States;
- (b) wholesale money market;
- (c) units in a collective investment scheme (including shares in an open-ended investment company);
- (d) contracts for differences other than equity index options and futures;
- (e) currencies;
- (f) commodities (including bullion);
- (g) life policies;
- (h) futures or options on any investment mentioned above;
- (i) issuing market allotments and syndication;
- (j) repurchase or reverse repurchase agreements, and stock or bond lending and borrowing; and
- (k) asset trading, including novation, assignment and sub-participation;

Details of the reporting system used should be provided to the Commission.

(3) Reports of transactions in accordance with (2) above must be made no later than the end of the business day following the date of the transaction, except that transactions in new instruments may be made on the day after the date of allotment or the day after the date on which the issue price is fixed, whichever is later.

(4) A firm does not have to report a transaction in accordance with (2) above where:

- (a) the firm, or another person sending the contract or similar note to the firm's customer, has reported that transaction to a qualifying exchange;¹⁶ or
- (b) the transaction is in a traded option, or a future, or an index option or future and has been executed on, and reported to, an appropriate qualifying exchange on behalf of the firm by a member of that exchange.

(5) The price reported must be the transaction price, excluding any charges which have been separately disclosed on the contract or similar note.

(6) One aggregate transaction may be reported for discretionary funds where allocation at the transaction price is made in a fixed ratio which has been notified to the Commission in advance.

¹⁶ In such instances details of the exchange(s) should be provided to the Commission.

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(7) A series of transactions executed within a 24 hour period which constitutes an exact replica of any of the following indices (known as a "basket trade") may be reported as a single transaction (in accordance with (3) above) under a single approved security code:

- (a) Nikkei 225
- (b) Standard and Poors 500
- (c) LSE/Nikkei 50
- (d) CAC 40
- (e) DAX 30, or
- (f) TOPIX.

(8) A transaction has been properly reported in accordance with (2) above only if the following mandatory fields can be properly implied or have been completed correctly, and the report has been accepted by the relevant reporting system:

- (a) the firm's identifying code;
- (b) the investment's identifying code of an approved security type;¹⁷
- (c) the date and time of the transaction;
- (d) the transaction size, price and currency;
- (e) whether the transaction is a purchase or sale;
- (f) whether the firm dealt as principal or agent;
- (g) the settlement date;
- (h) the counterparty's identifying code (where the reporting system permits);
- (i) the transaction's reference number; and
- (j) any other mandatory fields required by the reporting system.

(9) All reports must adhere to the codes and regulations laid down for the relevant reporting system in the appropriate documentation for that system.

(10) Exemptions from reporting or variations in the terms of reporting may be granted by the Commission for all firms, particular classes of firms, or specified firms, in particular transactions, particular series of transactions, or issues in specified investments or classes of investments.

(11) A firm may appoint a transaction reporting agent to make reports to the Commission on its behalf. Such reports should distinguish each individual transaction using the firm's identifying code. The firm should notify the Commission of any such arrangement, and will retain full responsibility for compliance with all reporting requirements.

(12) In the event of a prolonged central failure of an approved reporting system, the requirement to report transactions under (3) above by the end of the business day following their execution may be suspended by the Commission. A failure of a firm's own system, or that of its reporting agent, which prevents such reporting should be notified without delay to the Commission, which may agree a suspension of the reporting requirement or specify an alternative means of reporting.

COMPLIANCE

Guidance note

The Commission requires a firm to have adequate arrangements to ensure that its employees are suitable, adequately trained and properly supervised. The Commission would expect the arrangement to cover recruitment, including the vetting of applicants for employment and the taking up of references.

¹⁷ Details of the security types should be provided to the Commission.

Personal and other dealings**Responsible behaviour in personal and other dealings**

202. (1) A firm must take reasonable steps, including the establishment and maintenance of procedures, to ensure that its officers and employee or agent act in conformity with:

- (a) their own and their employer's relevant responsibilities under the regulatory system;
- (b) where relevant, the requirements of the statutory restrictions on insider dealing; and
- (c) appropriate arrangements on propriety in personal dealings.

(2) A firm must give to every employee a written notice (the "Personal Account Notice") setting out the requirements of code 203 (1) below and it must ensure that every employee enters into a written undertaking with the firm to observe the requirements of the Personal Account Notice.

(3) A firm must designate its employees' own accounts, and any other accounts subject to the Personal Account Notice requirements, in a way which enables such accounts to be distinguished from other customers' accounts.

(4) A firm must ensure that the Personal Account Notice identifies the compliance officer or an employee of the firm designated by him to be responsible for receiving reports and granting permissions in respect of activities undertaken by its employees in accordance with the Personal Account Notice.

(5) A firm must establish and maintain compliance procedures and appropriate arrangements designed to ensure that no employee accepts any gift or inducement which is likely to conflict with his duties to any customer of the firm.

(6) (2) above does not apply to:

- (a) non-executive directors, except in respect of dealings in the securities of the firm or the firm's group, or investments related to such securities;
- (b) a temporary employee (not regularly employed by the firm) whom the firm reasonably believes will not be involved to any material extent in the firm's investment business;
- (c) an overseas employee, unless that employee is to be based in the Isle of Man for any period of 30 days or more within any 12 month period.

Personal Account Notice

203. (1) The Personal Account Notice must require that an employee:

- (a) does not deal for his own account in investments of any kind in which his firm carries on investment business to any material extent, or in any related investments, without the permission of his firm (such permission may be general or specific);
- (b) does not deal in investments for his own account with any of the firm's customers without the prior consent of the firm.
- (c) reports promptly to his firm in writing any transaction for his own account for which permission is required under (a) above which he enters into otherwise than through the firm (or an associate of the firm who is an authorised person, unless he has arranged for his firm to receive promptly a copy of the contract or similar note issued in respect of the transaction.
- (d) does not deal for his own account in an investment in circumstances where he knows or should know that the firm or an associate intends to publish a written recommendation, or a piece of research or analysis, in respect of that investment or any related investment which could reasonably be expected to affect the price of that investment;

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- (e) does not deal for his own account at a time or in a manner which he knows or should know is likely to have a direct adverse effect on the particular interests of any customer of the firm; and
- (f) does not accept any gift or inducement from any person which is likely to conflict with his duties to any customer of the firm.

(2) The Personal Account Notice must specify that the references to an employee dealing for his own account include an employee:

- (a) dealing in his capacity as a personal representative of an estate or as a trustee of a trust, in which estate or under which trust there is a significant interest held by the employee, or any associate of the employee, or any company or partnership controlled by him or by any associate of the employee;
- (b) otherwise dealing in his capacity as a personal representative or a trustee, unless he is relying entirely on the advice of another person from whom it is appropriate to seek advice in the circumstances; or
- (c) dealing for the account of another person unless he does so in the course of his employment with the firm.

(3) The Personal Account Notice must further state that, if an employee is precluded from entering into a transaction for his own account, he must not (except in the proper course of his employment):

- (a) procure any other person to enter into such a transaction; or
- (b) communicate any information or opinion to any other person if he knows, or has reason to believe, that the person will, as a result, enter into such a transaction, or counsel or procure some other person to do so.

(4) Code 203 (1) and (2) above do not apply to:

- (a) any transaction by an employee for his own account in a packaged product; and
- (b) any discretionary transaction entered into for, and without prior communication with the employee, provided that the discretion is not exercised by the firm.

(5) A firm may delegate its performance of the responsibilities under codes 201 (2) to 202 (4) above in respect of employees' personal and other dealings to an undertaking in the same group.

Compliance with statements

204. Where a firm is required under the Conduct of Business Codes to state that it has done or will do something, then it must ensure that it does so as stated. Similarly, a firm must refrain from doing anything which it is required under the Conduct of Business Codes to state that it has not done or will not do.

Compliance review

205. A firm must undertake annually a review of its business to enable it to determine the effectiveness of its compliance and monitoring procedures, and must report to the Commission the main conclusions of this review within four months of its annual accounting reference date or other review period previously agreed with the Commission.

Record keeping

206. (1) A firm must take reasonable steps, including the establishment and maintenance of procedures, to ensure that sufficient information is recorded and retained about its investment business and compliance with the regulatory system. Such records must be retained for a period of 6 years from the specified date.

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(2) Records required to be maintained by the regulatory system may be inspected by a person appointed for the purpose by the Commission and must be produced promptly to that person on request.

(3) All records made by a firm in accordance with (1) above may be recorded in any form, but must be capable of prompt reproduction in hard printed form in English.

(4) For the period during which it is required to keep the relevant records, a firm must make available to any, or any former, private customer or discretionary non-private customer on request, within a reasonable period:

- (a) those parts of any written material and records which relate to that customer and which the firm has sent, or is required to send, to that customer under the CoB Codes; and
- (b) copies of any correspondence received from that customer relating to investment business.

Appendix A

Warrants Risk Warning Notice - (code 174 (2))

This notice is provided to you, as a private customer, in compliance with the codes the Financial Supervision Commission (the Commission). Private customers are afforded greater protections under these codes than other customers, and you should ensure that your broker tells you what these are. This notice cannot disclose all of the risks and other significant aspects of warrants. You should not deal in them unless you understand the nature of the transaction you are entering into and the extent of your exposure to potential loss.

You should consider carefully whether warrants are suitable for you in the light of your circumstances and financial position. In deciding whether to trade, you should be aware of the following matters.

Warrants

- 1 A warrant is a right to subscribe for shares, debentures, loan stock or government securities, and is exercisable against the original issuer of the securities. **Warrants often involve a high degree of gearing, so that a relatively small movement in the price of the underlying security results in a disproportionately large movement in the price of the warrant. The prices of warrants can therefore be volatile.**

You should not buy a warrant unless you are prepared to sustain a total loss of the money you have invested plus any commission or other transaction charges.

Some other instruments are also called warrants but are actually options (for example, a right to acquire securities which is exercisable against someone other than the original issuer of the securities, often called a "covered warrant").

Off-Exchange Transactions

- 2 Transactions in off-exchange warrants may involve greater risk than dealing in exchange traded warrants because there is no exchange market through which to liquidate your position, to assess the value of the warrant or the exposure to risk. Bid and offer prices need not be quoted, and even where they are, they will be established by dealers in these instruments and consequently it may be difficult to establish what is a fair price.

Your broker must make it clear to you if you are entering into an off-exchange transaction and advise you of any risks involved.

Commissions and charges

- 3 Before you begin to trade you should have all the relevant facts relating to the firm's remuneration attributable to any transaction and details of any other charges for which you will be liable.

Foreign Markets

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- 4 Foreign markets will involve different risks to UK markets. In some cases the risks will be greater. On request, your broker must provide an explanation of the protections which will operate in any relevant foreign markets, including the extent to which he will accept liability for any default of a foreign broker through whom he deals. The potential for profit or loss from transactions on foreign markets will be affected by fluctuations in foreign exchange rates.

[Name of firm]

[On duplicate for signature by private customer]

I/we have read and understood the risk warning notice set out above.

Date _____

[Signature of Customer] _____

[Signature of Joint Account Holder] _____

Note to firms -

This notice may be incorporated as part of a two-way customer agreement, except that the customer must sign separately that he has read and understood the risk warnings.

Appendix B - Derivatives Risk Warning Notice And Generic Risk Disclosure Statement

Set out in this Appendix are two versions of the Derivatives Risk Warning Notice for use in accordance with code 174 (2).

The Generic Risk Disclosure Statement may be used as an alternative to the Commission Derivatives Risk Warning Notice. It may not be used as an alternative to the Warrants Risk Warning Notice in **Appendix A**.

DERIVATIVES RISK WARNING NOTICE

This notice is provided to you as a private customer in compliance with the Financial Supervision Commission (Stockbrokers) Regulatory Code. Private customers are afforded greater protections under these codes than other customers, and you should ensure that your broker tells you what these are. This notice does not disclose all of the risks and other significant aspects of derivatives products such as futures, options, and contracts for differences. **You should not deal in derivatives unless you understand the nature of the contract you are entering into and the extent of your exposure to risk. You should also be satisfied that the contract is suitable for you in the light of your circumstances and financial position.** Certain strategies, such as a "spread" position or a "straddle", may be as risky as a simple "long" or "short" position.

Whilst derivative instruments can be utilised for the management of investment risk, some investments are unsuitable for many investors. Different instruments involve different levels of exposure to risk, and in deciding whether to trade in such instruments you should be aware of the following points.

Futures

- 1 Transactions in futures involve the obligation to make, or to take, delivery of the underlying asset of the contract at a future date, or in some cases to settle your position with cash. **They carry a high degree of risk.** The "gearing" or "leverage" often obtainable in futures trading means that a small deposit or down payment can lead to large losses as well as gains. It also means that a relatively small market movement can lead to a proportionately much larger movement in the value of your investment, and this can work against you as well as for you. **Futures transactions have a contingent liability, and you should be aware of the implications of this, in particular the margining requirements, which are set out in paragraph (6) below.**

Options

- 2 There are many different types of options with different characteristics subject to different conditions:

Buying options:

Buying options involves less risk than selling options because, if the price of the underlying asset moves against you, you can simply allow the option to lapse. The maximum loss is limited to the premium, plus any commission or other transaction charges. However, if you buy a call option on a futures contract and you

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later exercise the option, you will acquire the future. This will expose you to the risks described under "futures" and "contingent liability transactions".

Writing options:

If you write an option, the risk involved is considerably greater than buying options. You may be liable for margin to maintain your position and a loss may be sustained well in excess of any premium received. By writing an option, you accept a legal obligation to purchase or sell the underlying asset if the option is exercised against you, however far the market price has moved away from the exercise price. If you already own the underlying asset which you have contracted to sell (known as "covered call options") the risk is reduced. If you do not own the underlying asset (known as "uncovered call options") the risk can be unlimited. **Only experienced persons should contemplate writing uncovered options, and then only after securing full details of the applicable conditions and potential risk exposure.**

Traditional options:

A particular type of option called a "traditional option" is written by certain London Stock Exchange firms under special exchange rules. These may involve greater risk than other options. Two way prices are not usually quoted and there is no exchange market on which to close out an open position or to effect an equal and opposite transaction to reverse an open position. It may be difficult to assess its value or for the seller of such an option to manage his exposure to risk.

Certain options markets operate on a margined basis, under which buyers do not pay the full premium on their option at the time they purchase it. In this situation you may subsequently be called upon to pay margin on the option up to the level of your premium. If you fail to do so as required, your position may be closed or liquidated in the same way as a futures position.

Contracts for differences

- 3 Futures and options contracts can also be referred to as a Contract for Differences. These can be options and futures on the FTSE 100 index or any other index, as well as currency and interest rate swaps. However, unlike other futures and options, these contracts can only be settled in cash. Investing in a contract for differences carries the same risks as investing in a future or an option and you should be aware of these as set out in paragraphs (1) and (2) respectively. **Transactions in contracts for differences may also have a contingent liability and you should be aware of the implications of this as set out in the paragraph (6) below.**

Off exchange transactions

- 4 It may not always be apparent whether or not a particular derivative is on or off-exchange. Your broker must make it clear to you if you are entering into an off exchange derivative transaction. Under the Financial Supervision Commission (Stockbrokers) Regulatory Code, off-exchange transactions which have a contingent liability (see paragraph 6) are only permitted where it is for the purpose of protecting your assets against currency fluctuations.

While some off-exchange markets are highly liquid, transactions in off-exchange or "non transferable" derivatives may involve greater risk than investing in on-exchange derivatives because there is no exchange market on which to close out an open position. It may be impossible to liquidate an existing position, to

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assess the value of the position arising from an off-exchange transaction or to assess the exposure to risk. Bid and offer prices need not be quoted, and, even where they are, they will be established by dealers in these instruments and consequently it may be difficult to establish what is a fair price.

Foreign markets

- 5 Foreign markets will involve different risks from UK markets. In some cases the risks will be greater. On request, your broker must provide an explanation of the relevant risks and protections (if any) which will operate in any relevant foreign markets, including the extent to which he will accept liability for any default of a foreign broker through whom he deals. The potential for profit or loss from transactions on foreign markets or in foreign denominated contracts will be affected by fluctuations in foreign exchange rates.

Contingent liability transactions

- 6 Contingent liability transactions which are margined require you to make a series of payments against the purchase price, instead of paying the whole purchase price immediately.

If you trade in futures, contracts for differences or sell options you may sustain a total loss of the margin you deposit with your broker to establish or maintain a position. If the market moves against you, you may be called upon to pay substantial additional margin at short notice to maintain the position. If you fail to do so within the time required, your position may be liquidated at a loss and you will be liable for any resulting deficit.

Even if a transaction is not margined, it may still carry an obligation to make further payments in certain circumstances over and above any amount paid when you entered the contract.

Except in specific circumstances under Financial Supervision Commission (Stockbrokers) Regulatory Code, your broker may only carry out margined or other contingent liability transactions with or for you if they are traded on or under the rules of a recognised or designated investment exchange. Contingent liability transactions which are not traded on or under the rules of a recognised or designated investment exchange may expose you to substantially greater risks.

Collateral

- 7 If you deposit collateral as security with your broker, the way in which it will be treated will vary according to the type of transaction and where it is traded. There could be significant differences in the treatment of your collateral depending on whether you are trading on a recognised or designated investment exchange, with the rules of that exchange (and associated clearing house) applying, or trading off exchange. Deposited collateral may lose its identity as your property once dealings on your behalf are undertaken. Even if your dealings should ultimately prove profitable, you may not get back the same assets which you deposited and may have to accept payment in cash. You should ascertain from your broker how your collateral will be dealt with.

Commissions and charges

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- 8 Before you begin to trade, you obtain all the relevant facts relating to the firm's remuneration attributable to any transaction and details of any other charges for which you will be liable. If any charges are not expressed in money terms (but, for example, as a percentage of contract value), you should obtain a clear written explanation, including appropriate examples, to establish what such charges are likely to mean in specific money terms. In the case of futures, when commission is charged as a percentage, it will normally be as a percentage of the total contract value, and not simply as a percentage of your initial payment.

Suspensions of trading

- 9 Under certain trading conditions it may be difficult or impossible to liquidate a position. This may occur, for example, at times of rapid price movement if the price rises or falls in one trading session to such an extent that under the rules of the relevant exchange trading is suspended or restricted. Placing a stop-loss order will not necessarily limit your losses to the intended amounts, because market conditions may make it impossible to execute such an order at the stipulated price.

Clearing house protections

- 10 On many exchanges, the performance of a transaction by your broker (or the third party with whom he is dealing on your behalf) is "guaranteed" by the exchange or its clearing house. However, this guarantee is unlikely in most circumstances to cover you, the customer, and may not protect you if your broker or another party defaults on its obligations to you. On request, your broker must explain any protection provided to you under the clearing guarantee applicable to any on-exchange derivatives in which you are dealing. There is no clearing house for traditional options, nor normally for off-exchange instruments which are not traded under the rules of a recognised or designated investment exchange.

Insolvency

- 11 Your broker's insolvency or default, or that of any other brokers involved with your transaction, may lead to positions being liquidated or closed out without your consent. In certain circumstances, you may not get back the actual assets which you lodged as collateral and you may have to accept any available payment in cash. On request, your broker must provide an explanation of the extent to which he will accept liability for any insolvency of, or default by, other brokers involved with your transactions.

[Name of Firm]

[On duplicate for Signature by private customer]

I/We have read and understood the risk warning notice set out above.

Date _____

[Signature of Customer] _____

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[Signature of Joint Account Holder] _____

Note to firms

Paragraphs 1-7 may be deleted when they relate to particular kinds of business which will not be carried out with or for the customer. Paragraphs 8-11 are mandatory and may not be deleted.

Firms may also include descriptions of the types of investments covered by this notice, provided such descriptions do not lessen the effect of the risk warnings provided.

This notice may be incorporated as part of a two-way customer agreement, except that the customer must sign separately that he has read and understood the risk warnings.

GENERIC RISK DISCLOSURE STATEMENT

Risk Disclosure Statement for Futures and Options

This brief statement does not disclose all of the risks and other significant aspects of trading in futures and options. In light of the risks, you should undertake such transactions only if you understand the nature of the contracts (and contractual relationships) into which you are entering and the extent of your exposure to risk. Trading in futures and options is not suitable for many members of the public. You should carefully consider whether trading is appropriate for you in light of your experience, objectives, financial resources and other relevant circumstances.

Futures

Effect of 'Leverage' or 'Gearing'

1. Transactions in futures carry a high degree of risk. The amount of initial margin is small relative to the value of the futures contract so that transactions are 'leveraged' or 'geared'. A relatively small market movement will have a proportionately larger impact on the funds you have deposited or will have to deposit: this may work against you as well as for you. You may sustain a total loss of initial margin funds and any additional funds deposited with the firm to maintain your position. If the market moves against your position or margin levels are increased, you may be called upon to pay substantial additional funds on short notice to maintain your position. If you fail to comply with a request for additional funds within the time prescribed, your position may be liquidated at a loss and you will be liable for any resulting deficit.

Risk-reducing orders or strategies

2. The placing of certain orders (e.g. 'stop-loss' orders, where permitted under local law, or 'stop-limit' orders) which are intended to limit losses to certain amounts may not be effective because market conditions may make it impossible to execute such orders. Strategies using combinations of positions, such as 'spread' and 'straddle' positions may be as risky as taking simple 'long' or 'short' positions.

Options

Variable degree of risk

3. Transactions in options carry a high degree of risk. Purchasers and sellers of options should familiarise themselves with the type of option (i.e. put or call) which they contemplate trading and the associated risks. You should calculate the extent to which the value of the options must increase for your position to become profitable, taking into account the premium and all transaction costs.

The purchaser of options may offset or exercise the options or allow the options to expire. The exercise of an option results either in a cash settlement or in the purchaser acquiring or delivering the underlying interest. If the option is on a future, the purchaser will acquire a futures position with associated liabilities for margin (see the section on Futures above). If the purchased options expire worthless, you will suffer a total loss of your investment which will consist of the option premium plus transaction costs. If you are contemplating purchasing deep-out-of-the-money options, you should be aware that the chance of such options becoming profitable ordinarily is remote.

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Selling ('writing' or 'granting') an option generally entails considerably greater risk than purchasing options. Although the premium received by the seller is fixed, the seller may sustain a loss well in excess of that amount. The seller will be liable for additional margin to maintain the position if the market moves unfavourably. The seller will also be exposed to the risk of the purchaser exercising the option and the seller will be obligated to either settle the option in cash or to acquire or deliver the underlying interest. If the option is on a future, the seller will acquire a position in a future with associated liabilities for margin (see the section on Futures above). If the option is 'covered' by the seller holding a corresponding position in the underlying interest or a future or another option, the risk may be reduced. If the option is not covered, the risk of loss can be unlimited.

Certain exchanges in some jurisdictions permit deferred payment of the option premium, exposing the purchaser to liability for margin payments not exceeding the amount of the premium. The purchaser is still subject to the risk of losing the premium and transaction costs. When the option is exercised or expires, the purchaser is responsible for any unpaid premium outstanding at that time.

Additional risks common to futures and options

Terms and conditions of contracts

4. You should ask the firm with which you deal about the terms and conditions of the specific futures or options which you are trading and associated obligations (e.g. the circumstances under which you may become obligated to make or take delivery of the underlying interest of a futures contract and, in respect of options, expiration dates and restrictions on the time for exercise). Under certain circumstances the specifications of outstanding contracts (including the exercise price of an option) may be modified by the exchange or clearing house to reflect changes in the underlying interest.

Suspension or restriction of trading and pricing relationships

5. Market conditions (e.g. illiquidity) and/or the operation of the rules of certain markets (e.g. the suspension of trading in any contract or contract month because of price limits or 'circuit breakers') may increase the risk of loss by making it difficult or impossible to effect transactions or liquidate/offset positions. If you have sold options, this may increase the risk of loss.

Further, normal pricing relationships between the underlying interest and the future, and the underlying interest and the option may not exist. This can occur when, for example, the futures contract underlying the option is subject to price limits while the option is not. The absence of an underlying reference price may make it difficult to judge 'fair' value.

Deposited cash and property

6. You should familiarise yourself with the protections accorded money or other property you deposit for domestic and foreign transactions, particularly in the event of a firm insolvency or bankruptcy. The extent to which you may recover your money or property may be governed by specific legislation or local rules. In some jurisdictions, property which had been specifically identifiable as your own will be pro-rated in the same manner as cash for purposes of distribution in the event of a shortfall.

Commission and other charges

7. Before you begin to trade, you obtain all the relevant facts relating to the firm's remuneration attributable to any transaction and details of any other charges for which you will be liable. These charges will affect your net profit (if any) or increase your loss.

Transactions in other jurisdictions

8. Transactions on markets in other jurisdictions, including markets formally linked to a domestic market, may expose you to additional risk. Such markets may be subject to regulation which may offer different or diminished investor protection. Before you trade you should enquire about any rules relevant to your particular transactions. Your local regulatory authority will be unable to compel the enforcement of the rules of regulatory authorities or markets in other jurisdictions where your transactions have been effected. You should ask the firm with which you deal for details about the types of redress available in both your home jurisdiction and other relevant jurisdictions before you start to trade.

Currency risks

9. The profit or loss in transactions in foreign currency-denominated contracts (whether they are traded in your own or another jurisdiction) will be affected by fluctuations in currency rates where there is a need to convert from the currency denomination of the contract to another currency.

Trading facilities

10. Most open-outcry and electronic trading facilities are supported by computer-based component systems for the order-routing, execution, matching, registration or clearing of trades. As with all facilities and systems, they are vulnerable to temporary disruption or failure. Your ability to recover certain losses may be subject to limits on liability imposed by the system provider, the market, the clearing house and/or member firms. Such limits may vary: you should ask the firm with which you deal for details in this respect.

Electronic trading

11. Trading on an electronic trading system may differ not only from trading in an open-outcry market but also from trading on other electronic trading systems. If you undertake transactions on an electronic trading system, you will be exposed to risks associated with the system including the failure of hardware and software. The result of any system failure may be that your order is either not executed according to your instructions or is not executed at all.

Off-exchange transactions

12. In some jurisdictions, and only then in restricted circumstances, firms are permitted to effect off-exchange transactions. The firm with which you deal may be acting as your counterparty to the transaction. It may be difficult or impossible to liquidate an existing position, to assess the value, to determine a fair price or to assess the exposure to risk. For these reasons, these transactions may involve increased risks. Off-exchange transactions may be less regulated or subject to a separate regulatory regime. Before you undertake such transactions, you should familiarise yourself with applicable codes and attendant risks.

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Made this 3rd day of December 2003.

Commissioner

Chief Executive

EXPLANATORY NOTE

(This note is not part of the Code)

This Regulatory Code is made by the Financial Supervision Commission for the purpose of setting out the requirements that apply to holders of a Category 5 Investment Business Licence.

The Regulatory Code outlines general requirements; those relating to financial resources, systems, controls and reporting; requirements in relation to the handling of client money another assets and conduct of business.

This Regulatory Code replaces the Financial Supervision Commission (Stockbrokers) Regulatory Code 2003 which in turn replaced the Financial Supervision Commission (Stockbrokers) Regulatory Code 1996.