

Consultation on the Review of Financial Services Legislation

Draft Financial Services Rule Book 2009,
Draft Regulated Activities Order 2009 and
Draft Financial Services (Exemptions) Regulations 2009

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Financial Supervision Commission Barrantee Oaseirys

CONTENTS

	Page No.	
Section 1	INTRODUCTION	1
Section 2	KEY CHANGES TO THE REGULATED ACTIVITIES ORDER	3
Section 3	KEY CHANGES TO THE EXEMPTION REGULATIONS	5
Section 4	KEY CHANGES TO THE RULE BOOK	8
Section 5	CHANGES TO OTHER LEGISLATION	17
Section 6	CONSULTATION	18
Appendix A -	DRAFT REGULATED ACTIVITIES ORDER 2009	
Appendix B -	DRAFT FINANCIAL SERVICES (EXEMPTIONS) REGULATIONS 2009	
Appendix C -	DRAFT FINANCIAL SERVICES RULE BOOK 2009	

Section 1 - INTRODUCTION

Draft Regulated Activities Order and Draft Financial Services (Exemption) Regulations

The Regulated Activities Order (“RAO”) is an essential piece of secondary legislation under the Financial Services Act 2008. It specifies and defines the activities which constitute "regulated activities", and sets out “exclusions” (i.e. activities which are not regulated activities).

The Financial Services (Exemption) Regulations (“Exemption Regulations”) set out exemptions for certain persons from the need to hold a licence under the Financial Services Act 2008. Exempted activity remains regulated activity but it can be performed without a financial services licence.

Changes to these pieces of legislation may mean that activities that were previously excluded or exempt from requiring a licence become licensable. Therefore, it is very important that anyone relying on an exemption or exclusion reads the changes thoroughly to ensure that any change to their position is understood.

Draft Financial Services Rule Book

The Financial Services Rule Book (“the Rule Book”) is an important and large piece of secondary legislation. It incorporates the detailed requirements that all of the Commission’s licenceholders must abide by.

The Rule Book came into effect in its entirety for new licenceholders from 1st August 2008 and for the existing licenceholders from 1st January 2009.

Supervision Division and the Policy and Legal Division maintain data concerning the interpretation of particular Rules, and also data on potential changes / additions etc. that may be needed to maintain the accuracy and functionality of the Rule Book, including those raised by licenceholders.

The issues being addressed in the update of the Rule Book are mainly corrections of cross references and other minor amendments, flushed out by practical use of the Rule Book. Additionally, there are some draft new Rules for e-money businesses and amendments to the client money requirements.

Other secondary legislation

Any changes to the Rule Book, RAO and Exemptions Regulations may have incidental effects on other pieces of secondary legislation under the Financial Services Act 2008. By virtue of the draft changes the Financial Services (“Not Fit and Proper”) Regulations 2008, the Financial Services (Fees) Order 2009 and the Financial Services (Civil Penalties) Regulations 2008 will also require some minor amendments.

It is anticipated that all amendments will become operational on 1 January 2010.

Revised versions of the RAO, Exemption Regulations and the Rule Book showing all proposed amendments in tracked changes are included in this consultation as Appendices. In addition, the more significant changes are highlighted in the sections below. This should assist with your navigation of the consultation and give some background into the reasons for these changes.

You may notice that the style and layout of the legislation has been modernised. In order to make the documents as clear as possible any changes that are simply reformatting or relate to style where the meaning is unchanged are not in tracked changes and have not be highlighted.

Section 2 – KEY CHANGES TO THE REGULATED ACTIVITIES ORDER (“RAO”)

A revised version of the RAO showing all proposed amendments (other than formatting or style changes) in tracked changes is included in this consultation as Appendix A.

References to sections of the Insurance Act 1986 have been updated throughout to sections in the Insurance Act 2008. Similarly, references to the Companies Acts 1931 to 2004 have been updated throughout to the Companies Acts 1931 to 2009 to reflect the coming into effect of the Companies (Amendment) Bill 2008 which is anticipated shortly.

Class 2 - Investment Business

Exclusion 2(g) - Corporate services

This exclusion has been reworded to clarify that persons holding a Class 4 financial services licence may only conduct activities falling within Class 2(1), (2), (3) or (5) if the activity also falls within Class 4.

Class 3 - Services to Collective Investment Schemes

A new sub-paragraph (13) has been inserted to the regulated activities to cover the activity of acting as a representative for the governing body of a scheme and to accept service of notices and other documents on its behalf.

Class 4 - Corporate Services

Exclusion 4(d) – Group transactions

The exclusion has been extended to cover a company acting as an officer of a company, where both companies are part of the same group.

In addition, reference to “officer” has been removed from (c) as it is considered that individuals fulfilling the role of an officer should either be exempted or licensed.

Exclusion 4(e) – Joint enterprises

This exclusion has been removed (together with its definition), and the subsequent exclusions renumbered accordingly, as it is not considered that it would be used by anyone. If this is not the case and it is considered that the exclusion should remain, it is important that this fact is drawn to the Commission’s attention as part of this consultation process.

Class 5 - Trust Services

Exclusion 5(c) – Joint enterprises

This exclusion has been removed (together with its definition), and the subsequent exclusions renumbered accordingly, as it is not considered that it would be used by anyone. If this is not the case and it is considered that the exclusion should remain, it is important that this fact is drawn to the Commission’s attention as part of this consultation process.

Class 6 - Money Transmission Services and e-money

The regulated activity of issuing e-money has been carved out from money transmission services and is contained in Class 6. The remaining money transmission services are now contained in Class 8.

The regulated activity of money transmission has been reworded to extend it to cover “any service or activity” involving money transmission “either directly or as agent”.

The exclusion for “Activities of certain persons” (exclusion 6(a)) has been moved to the Exemption Regulations as it is considered more appropriate that it is an exemption.

Class 7 – Management or Administration Services

The regulated activity has been reworded slightly to more accurately reflect the activity. Also an exclusion for a company which provides management or administration services to another company within the same group has been inserted to make the position more clear.

Section 3 – KEY CHANGES TO THE EXEMPTION REGULATIONS

A revised version of the Exemption Regulations showing all proposed amendments (other than formatting or style changes) in tracked changes is included in this consultation as Appendix B.

Class 2 - Investment Business

Exemption 2.4 – Enduring powers of attorney

This exemption has been widened to cover where an attorney has entered into a discretionary management agreement with a person authorised to undertake that activity by an overseas regulator rather than just a person authorised under the Financial Services and Markets Act 2000.

Exemption 2.7 – Nominee companies

Regulated activities falling within Class 2(1) have been removed from the exemption as it is considered that nominee companies would not undertake this activity.

Class 3 - Services to Collective Investment Schemes

Exemption 3.1 – Nominee companies

This exemption has been widened to cover regulated activities falling within Class 3(11).

Class 4 - Corporate services

This part of the Exemption Regulations has been significantly rewritten. It is therefore important that careful consideration is given to this part during the consultation process.

Following comments from industry relating to the existing exemptions relating to acting as a director, which were not exactly replicated from the Fiduciary Services Act 2005, the Commission has reconsidered how persons acting as a director should be dealt with.

- ~ The exemption for acting as a director of a domestic services company has been removed as it was difficult to identify whether certain services counted as “domestic”. Please note that other activities relating to domestic services remain (see below).

- ~ An additional exemption has been included for “professional directorships” (*exemption 4.1*) which are undertaken by a person who is either —
 - (a) an advocate or firm of advocates;
 - (b) a registered legal practitioner or a firm of registered legal practitioners;
 - (c) a member of one of the following bodies —
 - (i) the Institute of Chartered Accountants in England and Wales;
 - (ii) the Institute of Chartered Accountants of Scotland;
 - (iii) the Institute of Chartered Accountants in Ireland; or
 - (iv) the Association of Chartered Certified Accountants,

provided that the person adheres to any continuing professional development requirements of his professional body and is in good standing with that body.

- ~ An additional exemption has been included for “group officers” (*exemption 4.3*) to cover persons acting as a director or alternate director of companies within a group but with a limit of no more than three groups. This exemption has resulted in the exemption for “nominee services” being reduced to avoid duplication.
- ~ The de minimus level of acting as a director or alternate director of no more than 10 companies remains (*exemption 4.2*) although it is no longer proposed to discount directorships of regulated companies. Therefore such directorships would be counted towards the de minimus level. Another option could be to reinstate that provision and discount directorships of Isle of Man regulated companies, views on this point would be welcomed.

The effect of the above is that if you are acting as a director of a company in your professional capacity as an advocate, legal practitioner or accountant, there is no regulatory limit to the number of directorships which can be held although it is expected that each professional will set a limit based on their ability to meet their directors’ duties.

Alternatively, if you do not fall within the professional capacity, the limit is a maximum of 10 directorships plus the directorships of companies in a maximum of 3 groups.

The rationale for these changes is that it is considered that a person is either acting in a professional capacity, in which case, there is no need to regulate such persons, or a person is undertaking directorships by way of business and should be regulated, subject to the de minimus level and where the activity is undertaken for a number of companies in the same group. It is accepted that the number of directorships in a group could be significant which is why the group exemption is limited to no more than 3 groups.

Questions – Are the above changes to the exemption structure appropriate? What are your views on removing the discounting of directorships of Isle of Man regulated companies from the calculation of the de minimus level?

Exemption 4.6(4) – Company officers and employees

The reference to company secretary has been removed as this was included in error.

Exemption 4.7 – Domestic services

The reference to the regulated activities has changed to remove acting as officers of a company and to limit the exemption to specific classes of activity. In order to address some confusion with the interpretation of this exemption, there is also a change to the wording of “the supply of any goods or services in **or from** the Island” with the word “**made**” being removed to clarify the meaning.

Class 5 – Trust services

Exemption 5.1 – Nominee services

This has been renamed “Corporate trustees, protectors and enforcers” to accurately reflect its purpose and the classes of regulated activity have been corrected.

Exemption 5.4 – Trusteeships

This is a new exemption (similar to the Class 4 “professional directorships” exemption) which exempt trusteehips undertaken by a person who is either —

- (a) an advocate or firm of advocates;
- (b) a registered legal practitioner or a firm of registered legal practitioners;
- (c) a member of one of the following bodies —
 - (i) the Institute of Chartered Accountants in England and Wales;
 - (ii) the Institute of Chartered Accountants of Scotland;
 - (iii) the Institute of Chartered Accountants in Ireland; or
 - (iv) the Association of Chartered Certified Accountants,

provided that the person adheres to any continuing professional development requirements of his professional body and is in good standing with that body.

Exemption 5.5 – De minimus

This exemption has been extended to enforcers and protectors.

Class 8 – Money Transmission Services

Exemption 8.2 – Transactions with overseas persons

This is a new exemption for overseas persons where a permitted person acts as agent for the overseas person provided the conditions of the exemption are met.

Exemption 8.3 – Activities of certain persons

This is a new exemption. Previously the content was included in an exclusion in the RAO. However, it is considered that it is more appropriate to be an exemption.

Schedule 2 – Temporary Business Continuity Services

Following receipt of legal advice which advised that post the invention of electronic communication a Court may find that any regulated activity for the purposes of the RAO which is conducted via a server located on the Isle of Man is business being conducted in the Isle of Man for the purposes of section 4(2)(a) of the Financial Services Act 2008, this Schedule has been substantially re-written to cover the use of computer apparatus located in the Island which is used to transact any regulated activity either for temporary business continuity purposes or otherwise.

Question – does this amendment cause any issues to licenceholders?

Section 4 – KEY CHANGES TO THE RULE BOOK

A revised version of the Rule Book showing all proposed amendments (other than formatting or style changes) in tracked changes is included in this consultation as Appendix C.

I. PART 2

Financial statements (Class 1 only)

- I.1 The Commission considers that it is beneficial, given the international client base of many deposit takers in the Island, that the audited financial statements of a deposit taker should be published on the deposit taker's (or relevant group's) website. This publication can be in the form of abridged financial statements. Guidance to this effect was formally implemented earlier in 2009. Rules 2.26 and 2.29 have been amended to reflect this requirement.

Interim financial returns (Classes 2, 3 and 6 only)

- I.2 The profit and loss account required in Rule 2.42 (4)(b) currently covers a specified quarter (or 6 months) however, the draft change would be to revert to a cumulative account. This would be more consistent with the way that businesses are run and would also remove or simplify the annual reconciliation process of the 4 quarters.

Question - Do you consider that including a cumulative profit and loss accounts in the interim financial returns would be an improvement or are you happy to continue with the Rule as it stands?

Calculation of Net Tangible Assets and Liquid Capital Requirement (Classes 2, 3, 4, 5 and 6)

- I.3 The calculation of net tangible assets detailed in Part A of Schedule 2.3 has been amended to enable licenceholders to identify current profits or losses and dividends paid which were not provided for in the most recent audited financial statements. The Commission may require a licenceholder to adjust its capital and reserves figure where there has been a significant change since the audited balance sheet was prepared.

Calculation of liquid capital (Class 2 only)

- I.4 The Commission considers that for Class 2 licenceholders there should be a provision for indemnity commission claw back in the calculation of liquid capital. It is proposed that the level should be set at 5% of the commissions the licenceholder has received on indemnity terms during the previous year.

2. PART 3

Types of client bank account

- 2.1 A lack of licenceholder understanding of the types of client bank accounts and their potential financial effect on insolvency of a bank has been evident at the recent client money presentations given by the Commission. The Commission recognises that it is possible for doubt to arise as to whether an account for a single client is “separate” or “designated”. Such a situation can have possibly unintended financial consequences for the client concerned and indeed for other clients. It is therefore considered that the current rules are too complex and should be simplified.

The result of the suggested amendments is to reduce the types of client bank account to two – a general client bank account which will always be pooled in the event of a bank default and a specified client bank account, at a bank selected either by the client or the licenceholder which will always be outside the pooling arrangements in the event of a bank default.

Client money information sheet

- 2.2 **Rule 3.7** requires that client money information is given to a client before a licenceholder takes any client money from that client. The information in the sheet may be incorporated into the client agreement or terms of business. The information sheet is designed to inform clients about the risks associated with the different types of client bank account so that they can make the licenceholder aware of any preferences.

Specified client bank accounts

- 2.3 The Commission is of the opinion that it is preferable for Class 4 and 5 licenceholders to open individual company accounts / trust accounts for their clients rather than opening specified client bank accounts. Therefore, the Commission is inclined to restrict such accounts to Class 2 and Class 3 only.

Question - Do Class 4 and Class 5 licenceholders consider that specified client bank accounts would be worthwhile for their clients and if so please specify how and why this is the case?

Chapter 3 – purposes for which client money is held

- 2.4 This chapter currently does not apply to Class 4 and Class 5 licenceholders as the majority of the requirements were not originally contained in the Fiduciary Services (Clients' Money and Trust Money) Regulatory Code. The Commission considers that these requirements are important for the proper protection of clients' money; therefore, it is proposed to bring them in for Class 4 and 5 licenceholders. The application of this chapter would also bring in the pooling arrangements for general client bank accounts.

- 2.5 Some licenceholders have suggested that pooling of client money should be limited to general client bank accounts and that subscription and redemption accounts (for collective investment schemes) should be moved outside the pooling arrangements. The Commission has issued a modification of this Rule to some Class 3 licenceholders.

Question - Should Rule 3.20 be amended to ensure that all subscription and redemption client accounts operated by Class 3 licenceholders will also be outside the pooling arrangements.

- 2.6 Rule 3.20 on pooling of client money has been extended to clarify how monies received from a compensation scheme or liquidation should be treated if clients' money has been pooled after the event of a bank default. This will probably require extra guidance to clarify that any compensation or liquidation proceeds should be applied to the benefit of all clients who have suffered reduction even if their money was not in the client account at the bank in default.

Interest on client money

- 2.7 **Rule 3.14** relating to interest on client money currently does not apply to Class 3 licenceholders. The Commission considers that for subscriptions awaiting the next dealing day, there should be an obligation upon the licenceholder to ensure that the subscribers are aware of the terms upon which the money is held. Typically there should be a paragraph of disclosure within the offering document, scheme particulars, prospectus or private placement memorandum. Rule 3.14 has been modified so that it captures this obligation for Class 3 licenceholders as well as for Class 2 and Class 4 licenceholders.

Reduced Client Money Requirement Option

- 2.8 **Rule 3.15A to 3.15F** relate solely to stockbrokers and reinsert requirements previously contained within the Stockbrokers Regulatory Code. These rules allow stockbrokers to offset positive individual customer balances with negative customer equity balances (or vice versa).

3. PART 6

Advertising

- 3.1 Rule 6.14 states the rubric to be used when referring to licensing in advertisements and on other documents. This has become very long and complex for some licenceholders who carry on several classes of regulated activity. It has been suggested that either:
- (a) for all advertising and documents the requirement to list each activity could be dropped so that all licenceholders could simply use "Licensed by the Isle of Man Financial Supervision Commission for financial services business"; or
 - (b) a short version of the rubric ("Licensed by the Isle of Man Financial Supervision Commission") could be introduced just for radio or television broadcasting, retaining the current requirement for any other advertising or documents.

- Questions*
- *Do you agree that a shorter version of the rubric is required?*
 - *Which of the above options would you consider to be most preferable?*

3.2 It is intended that a new Rule (6.17A) should be included for Class I licenceholders regarding reference to group ownership in advertisements. Guidance containing similar principles to this Rule was issued during 2009. The Commission considers that this information should be made available to clients of Class I licenceholders, especially in the current climate, and so it is proposed that a Rule be included to formalise this. The descriptive elements will remain in guidance to provide flexibility.

Statistical information (Classes 2, 3, 4 and 6 only)

3.3 Rule 6.58 on the provision of statistical information on collective investment schemes has been widened so that it applies to other statistical information required from Classes 2, 3 and 4. Please note that in order to apply this Rule to the different classes of licenceholder Rules 6.58 and 6.61 have been switched over.

It is envisaged that for Classes 2 and 3 the types of statistics to be provided will be –

- assets under management or custody at period end,
- split of business / assets under management or custody,
- number of clients, and
- split of clients into retail, non-retail and schemes by number and value, as appropriate.

For Class 4 (administration services to closed ended investment companies) the types of statistics to be provided will be –

- name, legal constitution, domicile, asset category, total and net assets of company,
- total value of subscription and redemptions,
- number of unit holders,
- approx % of unitholders (IOM/UK/Other EC/ Rest of the world),
- whether it is listed or unlisted, and
- name of NOMAD and custodian/prime broker.

For Class 6 (e-money issuers) the types of statistics to be provided will be –

- value of the client accounts at the start and end of the period, and
- turnover over the period.

The Commission will issue a list or table to be filled in as is currently the case for the collective investment schemes statistics. These will be requested quarterly.

Execution only business and limited advice (Class 2 only)

- 3.4 The Commission proposes to include definitions of “execution only” and “limited advice” in the Rule Book. The definition of execution only has been largely replicated from the definition contained in the previous Investment Business (Conduct of Business) Regulatory Code. It is also intended that if a licenceholder is carrying on execution only business some of the Rules contained in Part 6 (conduct of business) of the Rule Book should not apply to that business.
- 3.5 A new Rule has been inserted requiring licenceholders to confirm execution only or limited advice status in writing to the client and point out the consequent reduction of investor protection. Class 2 licenceholders who carry on these types of business are requested to look at this Part in detail and consider the proposed approach.

4. PART 8

Officers of licenceholders

- 4.1 Currently there is no requirement for compliance officers to be resident on the Island. It is proposed that Rule 8.18 should be extended to require all compliance officers to be resident on the Island.
- 4.2 It was suggested that MLROs and deputy MLROs should have the same unfettered access to all business lines and support departments as compliance officers under Rule 8.18(3); however, the Commission wants to stress the independence of the MLRO. The Rule has been amended to require that MLROs have unfettered access to all business lines and support departments and sufficient time and resources to discharge properly the responsibilities of the position.
- 4.3 **Rule 8.33** requires that for deposit takers incorporated in the Island at least one director must be of non-executive status. The Commission considers that an **independent** non-executive director should be required. In considering what constitutes independence in a non-executive director, the Commission would have regard to the Combined Code on Corporate Governance issued by the UK Financial Reporting Council, which can be found at <http://www.frc.org.uk/CORPORATE/COMBINEDCODE.CFM>

Professional indemnity insurance (“PII”)

- 4.4 Due to a number of issues and concerns about the level of required PII, the Commission has specifically reviewed the requirements on PII and carried out a comparison with Jersey, Guernsey and the UK, although a direct comparison is not fully possible because of the different ways that regulated activities are supervised in the separate jurisdictions). The Commission considers that –
- having a minimum level of PII of £250,000 is too low, particularly given the expense of legal costs;
 - it may appropriate to require branches to have PII cover to meet the local business rather than group business, however, it is suggested that this be balanced with a requirement to produce an auditors’ confirmation of the turnover of the Island business;

- the cap of £10m may be too high in some circumstances. It would seem reasonable to suggest that once a business reaches a certain size, turnover alone is not the catalyst that dictates an anticipated size of claim. The bigger picture would include claims history, number of transactions, spread of business and overall adherence to regulatory policy against the backdrop of a risk based approach. It may therefore be appropriate to consider a lower cap for certain types of business e.g. it is appropriate for a stockbroker, fund manager or fiduciary to have PII of £10m but it is recommended that the cap for financial advisers or promoters could be reduced to £5m;
- is not appropriate for professional officers to have PII, however it is appropriate that they have Directors and Officers Insurance and it is proposed that the level be £500,000;
- in calculating relevant turnover, dividend income should be excluded from the calculation but non-regulated activity income should be included in the calculation. As other activities may result in PII claims, it is considered that where a licenceholder is a mixed business, the income from such activity is relevant and the PII should be calculated on total income from both regulated and non-regulated activity;
- the Rules should require the following to be included in the policy and the licenceholder should be required to confirm on annual basis that the policy does indeed include -
 - ~ Breach of duty by reason of negligent act, error and omission;
 - ~ Cover to include libel or slander (to include former employees);
 - ~ Cover to include the dishonest or fraudulent act or omission by current and former employees; and
 - ~ Cover to include legal liability incurred by reason of loss of documents.

5. PART 9

Money Laundering and financing of terrorism

- 5.1 Most of the Rules in Part 9 have recently been incorporated into the Criminal Justice (Money Laundering) Code 2008 (“the Code”); therefore Part 9 of the Rule Book has been removed. Rule 9.3 is the only Rule that is not included in the Code so this Rule has been integrated into Part 6 of the Rule Book.

6. GENERAL

Notifications to the Commission

- 6.1 An addition has been made to rule 1.3 to clarify that requirements under the Rule Book, including the notifications, are in addition to those made under other legal requirements. The functions of the Commission (Registry or Regulator) are separate and so if one function is on notice of a situation, it does not follow that the other function is also aware. For example, the filing in the Registry of a form stating a director of a licenceholder has ceased to be in role, is not sufficient to provide the required regulatory notice of ceasing to act as a director (and vice versa) under the Rule Book. This rule will be accompanied by guidance which

clearly states that submissions to Companies Registry will not meet the submission requirements of the Rule Book.

- 6.2 Rule 6.59** requires Class 3 licenceholders to notify the Commission within 10 days of entering into an agreement to provide management or administration services to an overseas scheme. It is intended to modify the Rule so that the Commission must also be notified when a licenceholder ceases to provide services to an overseas scheme or when the information previously provided has changed.
- 6.3 Rule 7.7A** is a new Rule which requires a licenceholder to notify the Commission of any proposed pledge of, offer of options over or options granted in respect of any shares in the capital of the company. This has always been required by the general licensing policy; therefore, the Commission considers that it should not cause any issues for licenceholders.
- 6.4 Rule 7.12** requires that the Commission is notified if a licenceholder becomes aware of the service of notice or making of any order under the Criminal Justice Act 1990, the Criminal Justice Act 1991, the Drug Trafficking Act 1996 or the Anti-Terrorism and Crime Act 2003 against the licenceholder, an associated company of the licenceholder or any person for whom the licenceholder carries on any regulated activity. It is proposed to extend this to cover past customers for Class 4 and Class 5 licenceholders.
- 6.5 Rule 8.14** requires that all breaches of regulatory requirements should be notified to the Commission. The Commission considers that this Rule is too wide. In addition it is inconsistent with section 16 of the Annual Compliance Return which refers to confirming that all **material** breaches of the Rule Book have been notified. This Rule has been modified so that only material breaches need to be notified.
- 6.6 Rule 8.17** requires licenceholders to notify the Commission as soon as they become aware that certain things have occurred. The Commission proposes to add the following events to this list:
- any appeal made by the licenceholder to a Tribunal against any decision or action of the FSC; and
 - material loss of data.
- 6.7 Rule 8.57** requires notification of pricing errors by Class 3 licenceholders. The Commission considers that this Rule should be split so that errors over 0.5% of the price of a unit are notifiable to the Commission as soon as identified whereas errors below this threshold are reportable quarterly in arrears.

Other amendments

- 6.8** Rules 5.8 and 5.14 on management letters and the ISA 260 have been amended so that the position is more consistent for licenceholders incorporated in the Isle of Man and licenceholders incorporated outside the Isle of Man.
- 6.9** Rule 6.66 stated that where a company is struck off under section 273 or 319A of the Companies Act 1931 the records must be retained for not less than 13 years

to facilitate a request for restoration within the permitted 12 years. However, no reference was made to section 273A. It is considered that section 273A should be included for companies that are dissolved as there could still be a request for restoration within the 12 year period. A similar Rule for companies incorporated under the Companies Act 2006 has also been added. References to section 319A (of the Companies Act 1931) have been removed from this Rule as there are no restoration provisions within this section. Rule 8.25 relating to records of clients companies has similarly been amended.

6.10 Some new definitions have been included in Schedule I.1. These include –

- corporate officer and corporate trustee, enforcer or protector, which will enable a company whose business consists solely of acting as a director or secretary or as a trustee, enforcer or protector to be distinguished in the Rules from a nominee company;
- designated stock;
- execution only;
- limited advice;
- market counterparty, which has been taken from the now revoked Financial Supervision Commission (Stockbrokers) (No 2) Regulatory Code 2003;
- professional associate; and
- professional officer, which was previously defined in the Rules but was not sufficiently clear.

7. NEW RULES FOR E-MONEY ISSUERS

7.1 During 2007 the Commission consulted on implementing a regulatory regime for e-money issuers and money transmission services. There were a number of responses to the two consultations most of which were supportive of the principles. Since January 2009 all money transmission services have become licensable as Class 6 regulated activity and have been expected to comply with the Criminal Justice (Money Laundering) Code, Part 9 of the Rule Book (AML) and the AML Handbook.

7.2 E-money has been given a separate class of regulated activity. Class 6 has been amended to become E-money issuers only, with other money transmission services moving into Class 8. It is proposed to apply further Rules relating to, for example, holding clients' money, segregation of that money and reporting. The Commission proposes to enhance the regulatory regime for e-money issuers to cover:

Part 2 – Financial resources

Chapters 1, 7 and 8 will apply to all e-money issuers and Chapters 2 and 3 will apply as appropriate. This chapter applies financial resources requires to e-money issuers. Licenceholders will be expected to have £250,000 of share capital and net tangible assets as a minimum. These requirements will help to maintain licenceholders as a viable going concern and to overcome expected and unexpected difficulties.

Part 3 – Client money

The Commission expects that at any stage when an e-money provider retains, even temporarily, funds on behalf of a customer pending remittance or payment, those funds are held in a general client bank account. The effect of this segregation is that customers' monies should not become intermingled with the e-money provider's own funds. A reconciliation, of what is owed to customers at any one time, can be more easily undertaken and should the e-money provider fail, customers' monies would remain separate and not form part of the company's own resources in a liquidation. To cover these requirements, the intention is that the relevant sections of Part 3 of the Rule Book will be extended to cover e-money providers.

Part 6 – Conduct of business (chapters 1, 4A, 5 and 8 only)

The objectives of this Part are to ensure that a person authorised to carry on regulated activities acts with high standards of integrity and complies with best market practice; acts with due skill, care and diligence in providing any service; and deals fairly with clients in any transaction entered into. In addition, the Part lays down general principles relating to advertisements to which licenceholders should adhere. The Commission does not require licenceholders to submit draft advertisements for approval prior to publication.

Chapter 6 includes new rules inserted for e-money issuers only. Rule 6.71 protects holders of e-money by restricting the financial loss he would suffer if he loses his e-money card or if the firm becomes insolvent. The purpose of Rule 6.72 is to ensure that licenceholders redeem on demand any e-money issued so that clients are able to get cash back if necessary and confidence in e-money as a product will be increased.

Part 7 - Administration

All of this Part will apply to E-money issuers with the exception of Rules 7.18, 7.20 and 7.21.

Part 8 – Risk Management and Internal control (chapter 1 and Rule 8.54 only)

The Commission intends to apply chapter 1 and Rule 8.54 of Part 8 to Class 8 licenceholders. This will require a licenceholder to organise and control its internal affairs in a responsible manner. It is considered that licenceholders should be able to demonstrate to the Commission that they have in place documented control systems and procedures, which are appropriate to the level and scope of its business. In addition, they should be able to demonstrate the existence of adequate risk management systems, including insurance.

Section 5 - CHANGES TO OTHER LEGISLATION

3.1 Financial Services (“Not Fit and Proper”) Regulations 2008

It is the Commission’s policy to only list individuals who are currently subject to a “not fit and proper” direction and to remove the names from the register when the direction is revoked. However, this is not clear from the Regulations.

Therefore, it is proposed to amend these Regulations to clarify that the register held will only show current directions.

3.2 Financial Services (Civil Penalties) Regulations 2008

3.2.1 The Financial Services (Civil Penalties) Regulations 2008 were a consolidation of the provisions in the Civil Penalties Regulations issued under the Banking Act 1998, the Investment Business Acts 1991 to 1993 and the Fiduciary Services Acts 2000 and 2005. However, the penalty for deposit takers incorporated outside the Island relating to late submission of their Auditors’ Management Letter was omitted. The Commission considers that a consistent approach should be taken; therefore, this requirement will be reinstated. In addition, the penalty will be widened so that it applies to all licenceholders incorporated outside the Island in 2010.

3.2.2 The civil penalties do not currently apply to the audit report on banking returns (Rule 5.16) which should be submitted within 4 months of the year end. The Commission considers that a penalty should be applied for breach of this provision. The Regulations will be amended to reflect this position only for deposit takers.

3.3 Financial Services (Fees) Order 2009

3.3.1 As mentioned above, e-money and money transmission services have been split into Class 6 and Class 8 respectively. The Fees Order will be amended to reflect this position and the annual fee for e-money issuers will be increased to £9,950.

3.3.2 In addition, the split of activities in Class 2 will be broken down further. The Commission has identified some combinations of activities that currently fall within “Class 2 in any other case” which could be singled out and given a different fee as they are more common than expected. Business falling within Class 2 paragraphs (3) and (5) or paragraphs (3), (4), (5) and (7) will attract a fee of £3,750 as this is more proportionate to the activities undertaken.

Section 6 – CONSULTATION

It would be appreciated if we could have your comments as soon as possible. The closing date for comments is 10th August 2009.

Responses to: Mrs Shirley E Corlett
Senior Adviser - Policy & Legal Division
Financial Supervision Commission
PO Box 58
Finch Hill House
Bucks Road
Douglas IM99 IDT

Tel: (01624) 689323 E-mail: shirley.corlett@fsc.gov.im

The purpose of consultation is to obtain views and gather evidence from which to take an informed decision on the content of proposed legislation. A response to this consultation will not necessarily guarantee a change to that which is proposed.

A summary of the comments received with the Commission's response will be published on the Commission's website after all comments have been considered.